

DC DIMENSIONS

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More than 70 years after it was founded, the Plan Sponsor Council of America continues to protect, promote, and improve the US retirement system.

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Financial Wellness: Key Answers for Plan Sponsors

What should be the goal, scope, and desired outcome of a cost-effective benefits program focused on financial health?



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Letter from the Editor

Have you ever wondered about the origins of today's defined contribution system? How about the history, people, and inflection points that define how America now saves for retirement? Our feature story on the Plan Sponsor Council of America (PSCA) explores these questions and illuminates how and why this all-volunteer nonprofit organization has been plan sponsors' voice in Washington for over 70 years. We hope you, as a reader of *DC Dimensions*, similarly support this organization's goals of helping to protect, promote, and improve our retirement system.

In our DC Research section, we outline how Dimensional can provide assistance as you create an investment menu for plan participants who are focused solely on fees.

Advisors may find useful insights in our interview with MIT's Antoinette Schoar, PhD, who explains why advisors who are fiduciaries provide less-biased advice to their clients.

On the academic front, we check in with Zvi Bodie, PhD, Professor Emeritus at Boston University, who discusses the role of employers in improving the financial health of plan participants. Please be on the lookout for events featuring Zvi later this year (and in 2019) as we highlight how our global retirement solutions can be applied in the US.

It's no secret that defined contribution plans can be used for more than just saving for retirement. John D. Calaway, a Senior Gift Planning Officer at the University of San Francisco, lays out key considerations when making a bequest to heirs, charity, or institutions. After consulting with my own advisor, I updated my DC plan beneficiary designation form to, in part, name my alma mater, USF, as a beneficiary.

Last year we dedicated a lot of time to financial wellness. In this issue, we advance that effort with consultant Tony Verheyen's in-depth article on how to implement a financial wellness program.

Finally, Ian Kopelman, Partner for DLA Piper LLP (US), delivers an update on key fiduciary considerations when offering a health savings account.

Here is to better retirement outcomes for our all DC plan participants!

Sincerely,

A handwritten signature in black ink that reads "Timothy K. Kohn". The signature is fluid and cursive, with a long horizontal stroke at the end.

TIM KOHN,
*Head of DC Services and Vice President
Dimensional Fund Advisors*



PSCA

Voice of the Plan Sponsor

By **Tim Kohn**, Head of DC Services and Vice President
Dimensional Fund Advisors

More than 70 years after it was founded, the Plan Sponsor Council of America continues to protect, promote, and improve the US retirement system.

Early in the 20th century, during a time of rising socialism, a world at war, and global strife between employees and employers, sharing a company's profits with workers was a new and radical idea.

Against this backdrop, Robert S. Hartman, a young college professor, would garner support for a “new method of cooperation.”¹ His goal was to significantly improve relations in the workplace. Soon enough, Hartman organized what would be called the Council of Profit Sharing Industries. On June 13, 1947, in Cleveland, Ohio, 50 companies, mainly manufacturers like Pitney Bowes and S.C. Johnson & Son, met to create this seminal organization. Its remarkable mission: Strengthen free enterprise by extending profit sharing, spread prosperity through higher buying power and lower prices, and cultivate peace between workers and their bosses. Now 71 years old, the Plan Sponsor Council of America (PSCA) grew to become one of the key drivers of today's defined contribution system.

Who are the key people behind this organization, and how did it take on the all-important role of protecting, promoting, and improving the American retirement landscape? Here, we present a detailed look at the history, leadership, and impact of the PSCA, the voice of the plan sponsor. ►



“The PSCA is an invaluable resource for plan sponsors. The education, forum for discussion, and camaraderie have created a community dedicated to helping improve the retirement outcomes for all our plan participants.”

LEADERSHIP

The 22 officers and directors of the Plan Sponsor Council of America include members of both large and small companies as well as nonprofits that represent most sectors of the economy. The PSCA’s services are tailored to meet the needs of plan sponsors in organizations of all sizes. Together, these leaders serve as a resource to policy makers, the media, and other stakeholders as part of the PSCA’s commitment to improving retirement security for millions of Americans.

Officers and Directors

(back row, left to right)

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Robert Love
Treasurer,
Custom Air Products
& Services, Inc.

Stephen McCaffrey
Immediate Past
Chair, National
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Companies

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Evaluations, Inc.

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Principal
Resource Group

Tim Kohn
Dimensional
Fund Advisors

(Note: Directors
Monica Chen,
Ira Finn,
Colleen Houlihan,
Peter Kelly, and
William Shaw
are not pictured.)

▲ **SHIRLEY ZABIEGALA**
2nd Vice Chairperson,
PSCA; Director,
Savings and Retirement,
Nestlé USA, Inc.



HISTORY

Started in 1947, the Council of Profit Sharing Industries believed profit sharing might ease labor strife tied, in part, to reverberations from the Great Depression. In the ensuing decades, during wartime and administrations led by both parties, the PSCA was on the front lines as the US achieved key retirement security milestones.

Sources: PSCA; US Department of Labor; US Securities and Exchange Commission; Internal Revenue Service; Investment Company Institute Fact Book, 2013–2017; The Coalition of Collective Investment Trusts; ICI Research Fundamentals: “The US Retirement Market, 2006.”

1927

First collective trust funds created.

1929-1939 ▶

Great Depression

Florence Owens Thompson and her children in Nipomo, California, in 1936.



Source: The Library of Congress. loc.gov/item/2017762891/.

HISTORY



▲
DAVID WRAY



▲
ED FERRIGNO

Wray, Ferrigno Drive Key Reform Efforts

David Wray, former President, and Ed Ferrigno, former Vice President, Washington Affairs, at the PSCA were instrumental in leading the organization during key decades that helped to define the current defined contribution retirement system. Under their leadership, the PSCA was instrumental in helping to enact the Economic Growth Tax Relief Reconciliation Act of 2001 (EGTRRA) pension reform legislation as well as in efforts to obtain regulatory and legislative provisions that removed barriers and provided incentives for automatic enrollment plans. Automatic enrollment and EGTRRA permanence were both later included in the Pension Protection Act of 2006.

RECOGNITION

Women's Champion Cindy Hounsell Receives Lifetime Achievement Award



▲
CINDY HOUNSELL

President, Women's Institute for a Secure Retirement

The PSCA Lifetime Achievement Award, established in 2015, honors individuals who have made important contributions to the growth of the defined contribution industry. The goal is to celebrate contributions comprising the highest degree of technical expertise, innovation, philanthropy, and positive impact on the plan sponsor community, all of which help to create better retirement outcomes for the American DC plan participant.

Cindy Hounsell, the 2018 winner, is the President of WISER, the Women's Institute for a Secure Retirement.

"I have known Cindy for many years and continue to be impressed by her incredible dedication and heart for helping women navigate the many obstacles to a secure retirement," says nominator Annette Grabow, Retirement Plans Program Manager at Sonepar USA. "WISER's mission is personified in Cindy's efforts. ... Her contributions have not been limited to the plan sponsor community but cover the

broader retirement landscape. Plan sponsors benefit from her work and resources."

Hounsell, an attorney and retirement expert, has testified before Congress and served as a delegate for a number of White House Summits and conferences. She provides technical assistance to several national organizations as well as training to leaders and grassroots advocates as director of the National Resource Center for Women and Retirement Planning, funded by the US Administration on Aging.

"Cindy is the perfect fit for our Lifetime Achievement Award," says Jack Towarnicky, Executive Director of the PSCA. "She's a recognized leader positively affecting policy and the changing views in the retirement community. Her specific focus on helping women achieve their financial goals benefits all workers and their families, actively employed or already retired, regardless of gender."

1933
Securities Act of 1933

1933
Banking Act of 1933 (Glass-Steagall)

1934
US Securities and Exchange Commission established.

1935
Social Security Act

1939-1945 ▶
World War II

Joseph Stalin, Franklin D. Roosevelt, and Winston Churchill meet in Tehran, Iran, in late 1943.

1947
Council of Profit Sharing Industries created.



COMMITTEES

PSCA's Standing Committees Provide Ideas, Tools Behind Value Proposition

The PSCA is a volunteer-driven organization whose membership consists of many of America's leading benefits professionals—lawyers, human resources professionals, investment professionals, and others. Members of the standing committees, who donate their time, generate much of the intellectual capital, tools, and materials that deliver value to PSCA's plan sponsors. Below are highlights of the various committees, their missions, and key value adds:

HSA Committee

Formed based on the increasingly popular trend of offering a high deductible health plan (HDHP) along with the required health savings account, the committee educates members on the role of HSAs in overall benefits packages, best practices, and how to examine HSAs as both an insurance offering and a long-term health savings tool.

“Our committee was instrumental in impacting key legislation like EGTRRA, the Pension Protection Act, the US Department of Labor fiduciary rule and ... the fight against ‘Rothification’ of DC plans. ... Rulemakers and regulators appreciate the unique voice of employers that we bring to the debate.”

▲
STEPHEN MCCAFFREY
Chairman, PSCA
Legal and Legislative
Committee; Senior
Council, National Grid
USA Service Co., Inc.



Legal and Legislative Committee

The committee's primary mission is to provide the PSCA perspective in Washington on sound retirement policy in the regulatory and legislative areas. Quarterly meetings and numerous sub-committee meetings drive the agenda.

Education and Communication Committee

By providing members access to leading-edge, high quality communication and financial education materials and ideas, this committee tries to help company-sponsored profit sharing/401(k) plans to positively influence employer profitability and to improve employee use and appreciation for their plan.

Retirement Industry Advisory Committee (RIAC)

The continuing goals of this committee are to (1) help expand PSCA membership, (2) enable the PSCA to track and, where possible, influence governmental practices and policy toward DC plans, (3) drive PSCA's message in the national press by reinforcing issues important to the formation and preservation of DC plans in the service provider and plan sponsor community, and (4) maintain a meaningful dialogue with the PSCA on the views of the service provider community. “Plan sponsors raise ideas or concerns, and our committee provides the industry perspective and vice versa,” says RIAC Chairman Neil Lloyd, Head of US DC and Financial Wellness Research at Mercer. “This healthy collaboration ... is helping to solve complex problems.”

1950-1953 ▼

Korean War and Armistice Agreement

American soldiers celebrate Korean War cease-fire.



1955-1975 ►

Vietnam War

American soldiers help an injured comrade in Vietnam in 1965.

1978

Revenue Act of 1978 creates Section 401(k) of Internal Revenue Code.



LEADERSHIP



▲
TONY VERHEYEN

Tony Verheyen Sets Stage for Growth

Tony Verheyen, former Executive Director and Board Member of the PSCA, led, transformed, and set the stage for future growth. His proactive actions, outreach, and passion were important to the development of numerous committees. Today's committee structure is the backbone of how the PSCA serves its member base.

National Conference Planning Committee

The committee is dedicated to bringing innovative topics, speakers, and content to the PSCA National Annual Conference, which presents legislative and regulatory updates, insights and trends, the latest academic research, and communications best practices. Conference speakers and topics are chosen solely on merit as opposed to sponsorship.

Research Committee

The committee identifies areas of investigation and develops surveys to document current plan practices and employee behaviors. The data provides an important backbone of real-world experience to support PSCA's legislative efforts. The primary focus of the research committee is the development of the annual benchmarking surveys (see page 8).

Investment Committee

Consisting of plan sponsors and providers with a shared interest in the latest trends, developments, and use of investments in employer-sponsored retirement plans, the committee discusses both theoretical and pragmatic issues relating to asset allocation, portfolio composition, and the adoption of target date funds and retirement income products. It seeks to expand perspectives through an active dialogue about investment vehicles designed to enable participants to achieve their retirement goals.

“The Investment Committee provides plan sponsors an opportunity to discuss topical issues raised by member firms. It provides me and others access to experts in areas such as investments whom we can not only lean on but also use as a sounding board for other relevant issues.”

▲
BRANDON DIERSCH
Group Portfolio Manager, Capital Markets, Treasury, Microsoft



Non-Qualified Deferred Compensation Committee

The committee meets monthly and is working toward relaunching an annual survey on non-qualified deferred compensation plans and creating a buyer's guide, best-practice guide, white papers, and presentations to benefit PSCA's members and the plan sponsor community.

1979

Johnson & Johnson begins creation of its 401(k) plan.

1981

IRS issues rules sanctioning use of employee salary reductions for retirement plan contributions.

1985

McDonald's becomes first company to implement automatic enrollment for its plan participants.

1986 ▶

Tax Reform Act of 1986, signed by Ronald Reagan in October, reduces maximum allowable annual 401(k) deferrals, making profit sharing more equitable for all employees.

President Reagan signs Tax Reform Act of 1986.

1993

First collective investment trust-based target date.





▲ From left: Nevin Adams, Kenneth Raskin, and Jack Towarnicky.

LEADERSHIP

Nevin Adams, Kenneth Raskin, Jack Towarnicky Lead Push to Help Educate Plan Sponsors

Nevin Adams, Chief of Marketing & Communications at the ARA, Kenneth A. Raskin, Chair of the PSCA, and Jack Towarnicky, Executive Director of the PSCA guide the organization in its effort to educate plan sponsor members using programs and services that help them solve real problems, create positive change, and better manage their company retirement plans.

RESEARCH

Benchmarking Surveys Inform Plan Sponsors About Key Trends

The PSCA is a leading provider of benchmarking surveys and the only organization to produce annual corporate, governmental, not-for-profit, and non-qualified DC plan surveys. Plan sponsors use these surveys to benchmark their retirement plans, while service providers, consultants, academics, and the media rely on the surveys to gain an understanding of key trends.



▲ Plan sponsors look to PSCA surveys for benchmarking.

“Our surveys ... often inform key trends and media stories and impact how plans structure their investment menu, advice provisions, and use of automaticity, as well as other plan design features.”

▲ HATTIE GREENAN
Director of Research and Communication, PSCA

1995
Profit Sharing/401(k) Council of America renamed.

1996
First mutual fund-based target date fund created.

1996
Small Business Jobs Protection Act allows safe harbor methods for satisfying nondiscrimination testing.

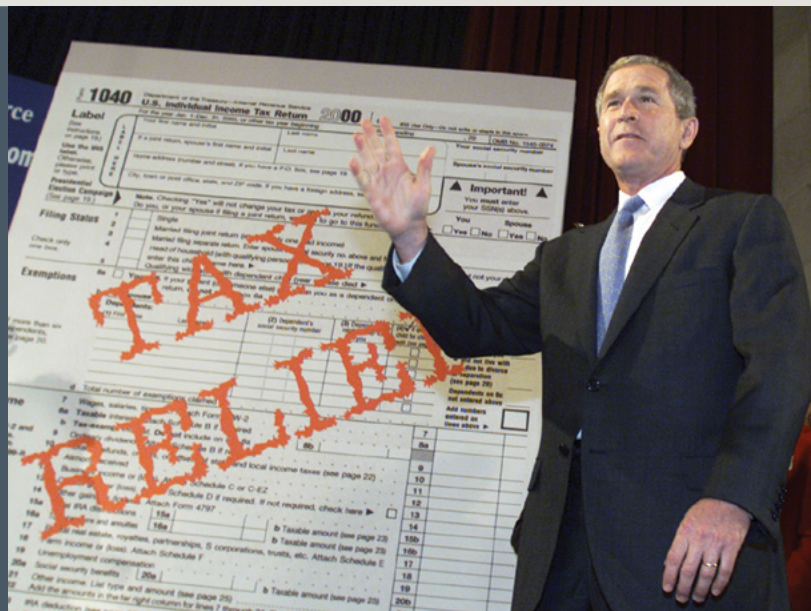
1998
Treasury Department, IRS issue a ruling clarifying that automatic enrollment in 401(k) plans is permissible for newly hired employees (Revenue Ruling 98-30).

2000
National Securities Clearing Corp. adds commingled investment trusts to mutual fund trading platform, Fund/SERV®.

2000
Target date fund assets hit \$9 billion.

2001 ▶
Economic Growth and Tax Relief Reconciliation Act (EGTRRA) allows for increased contribution, compensation, and deferral limits, plus catchup contributions and DC plan cashouts for those with under \$5,000 in account balances.

President Bush attends event in support of 2001 tax bill.



SUPPORT

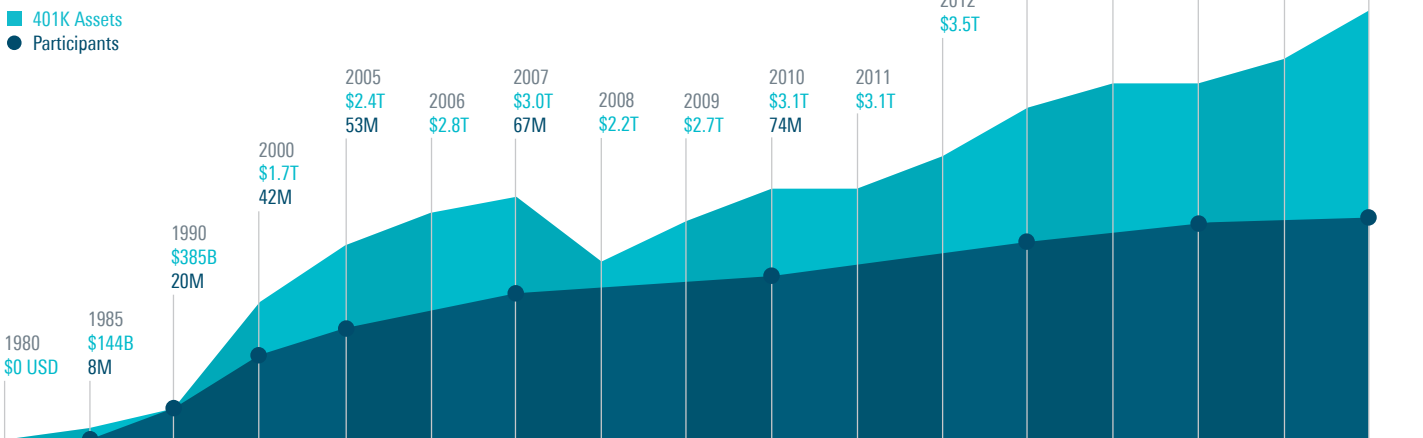
How Does PSCA Membership Benefit You?

Designed to inform, educate, and provide support, PSCA services are tailored to meet the needs of plan sponsors in organizations of all sizes. Membership benefits include:

- Legislative and regulatory updates
- Conferences
- Fiduciary training
- *Defined Contribution Insights*, a quarterly magazine focusing exclusively on the needs of employer-sponsored retirement plans
- Research and benchmarking
- Communications best practices
- Professional growth
- PSCA Signature Awards, designed to honor excellence in plan communication and investment education

For more information on PSCA, please call 312-419-1863, or visit: psca.org/membership-benefits.

Growth of 401(k) Assets and Participants 1980–2017



Sources: Investment Company Institute, US Department of Labor, Cerulli Associates. At the end of 2017, employer-sponsored DC plans—which include 401(k) plans, 403(b) plans, 457 plans, the federal Thrift Savings Plan (TSP), and other private-sector DC plans—held an estimated \$7.7 trillion in assets. With \$5.3 trillion at year-end 2017, 401(k) plans held the largest share of employer-sponsored DC plan assets, while 403(b) plans held another \$1 trillion. In addition, 457 plans and the federal Thrift Savings Plan (TSP) held a total of \$900 billion. Other private-sector DC plans without 401(k) features held the remaining \$500 billion.

2005
Target date fund assets hit \$71 billion.

2006 ▶
Pension Protection Act makes permanent some provisions of EGTRRA; law allows employers to automatically enroll employees under safe harbor into a DC plan when using a qualified default investment alternative (QDIA).



President Bush signs Pension Protection Act of 2006.

2007
IRS updates 403(b) regulations.

2007-2008 ▶
Considered by many economists as worst economic calamity since Great Depression, financial crisis leads to bailouts of several banks and global downturn in stock markets; DC plan participants' balances plunge to record lows.



The global financial crisis led to havoc in the stock market.

LOOKING AHEAD

What the Future May Hold

Predicting the future of America's defined contribution system is exceptionally difficult, especially when the regulatory process and breadth of stakeholders are considered. However, looking at the top concerns of PSCA members, as manifested in the Legal and Legislative Committee's projects, may help shed light on future trends, rules, and regulations that may further define how America saves for retirement. Read on for potential developments.

"Our future is brighter than ever, and I am honored to steward our efforts until we pass our passion on to the next generation of members. It is our members who truly make a difference in the lives of everyday Americans."

▲
KENNETH A. RASKIN
Chair, PSCA Board of Directors; Partner, King and Spalding LLP

Regulation

- SEC investment advice proposals.
- The Receiving Electronic Statements to Improve Retiree Earnings (RETIRE) Act and its goal to furnish participants with required statements and documents electronically.
- The Retirement Enhancement and Savings Act (RESA) and its lifetime income disclosures and safe harbor provisions.
- Legislation creating a safe harbor for plan sponsors when following the PSCA's 10-step process for locating "missing" participants.
- Expansion of the Self Correction Program under the Employee Plans Compliance Resolution System.

Plan Design

- Allowing not-for-profit, or 403(b) plans, access to invest in commingled investment trusts, just as their corporate and governmental plan counterparts can do today.
- RESA's proposals to broaden access to multiple employer plans (MEPs).

Investments

- Lifetime Income. Pending greater regulatory safe harbor provisions with respect to disclosure and use of annuities, solutions targeting retirement income may become more prevalent.
- Target Date Funds. As target date funds pass \$1 trillion in assets, representing over 20% of all DC plan participant holdings, a trend to watch is the increasing use of target date funds focused on income as the outcome.
- Managed Accounts. This space should continue to grow in terms of providers and participant use; a review of the PSCA's Managed Accounts Buyers Guide for evaluation considerations seems warranted.
- Environmental, Social, and Governance (ESG). Now a full-fledged focus for much of the industry and a top interest of PSCA member firms, funds emphasizing ESG are viewed as viable options that do not compromise on sound investment principles or expose investors to lower expected returns. The recently produced PSCA ESG Resource Guide highlights index, research, and investment solution providers.

2010
Department of Labor proposes a broadened definition of fiduciary, the "DOL Fiduciary Rule."

2010
Target date fund assets hit \$340 billion.

2011
Plan Sponsor Council of America renamed.



2012
American Taxpayer Relief Act of 2012 signed into law by President Obama, making permanent Bush era tax cuts and ending EGTRRA sunset provisions.

2013
Target date fund assets hit \$618 billion.

2014 ▶
IRS Notice 2014-66 allows for expanded use of certain annuities in 401(k) plans.



2016
DOL Fiduciary Rule issued, expanding "investment advice fiduciary" definition under ERISA.

2016
Target date fund assets cross \$1 trillion.

2017
PSCA becomes a founding member of Save Our Savings Coalition, an alliance dedicated to protecting Americans' retirement savings as Congress plans for and executes comprehensive tax overhaul.

LEADERSHIP



▲
KENNETH A. RASKIN



▲
BRIAN GRAFF

Kenneth Raskin, Brian Graff Unify Retirement Organizations

In late 2017, the PSCA voted to become a division of the American Retirement Association (ARA), and together they now represent 20,000 members. Kenneth A. Raskin, Chair, of the PSCA, and Brian Graff, CEO of the ARA, led both organizations in their efforts to join together to represent virtually every type of pension professional. That group includes plan sponsors, actuaries, consultants, insurance professionals, financial advisors, accountants, attorneys, and HR managers committed to protecting and improving America's private pension system.

2017

PSCA enters combination agreement with American Retirement Association.

2018

US Fifth Circuit Court of Appeals vacates DOL Fiduciary Rule; DOL fails to appeal; appeals by several states to Fifth Circuit denied.

2018

Securities and Exchange Commission proposes investment advice rule.

Thanks to America's voluntary, employer-sponsored retirement system, millions of plan participants have saved trillions of dollars for the future. The engine of that system, says David Wray, is the employer's involvement: "Employees trust their employers; they are key to the system working. Held to the highest standard of oversight, companies take on the fiduciary responsibility that defines our system and allows employees to forgo consumption for decades. That confidence comes only with the unwavering support of their employer."

Dimensional salutes the members of the PSCA and their companies for generously sharing their expertise across the DC industry.

1. Virginia Dawson, *The Creation of the Council of Profit Sharing Industries*. (PSCA), page 3.

Dimensional Founder and Executive Chairman David Booth and Tim Kohn, Dimensional's Head of Defined Contribution Sales, chair the PSCA Investment Committee. Kohn is also a member of the PSCA Board of Directors. Dimensional Fund Advisors and PSCA are unaffiliated entities.

Dimensional Fund Advisors LP receives compensation in the form of investment management fees from the following clients: Nestle USA, National Grid USA, and Microsoft.

Fees vs. Value: What Are You Taking Home?

Prudent fund selection should look beyond expense ratios and consider expected value to participants.

► By **Dave Twardowski, PhD**, Vice President, Research, and **Jerome Thornton**, Institutional Services
Dimensional Fund Advisors

For most consumers, costs matter with any purchase they make. However, costs are rarely the only consideration. Whether they are buying shoes, a car, or even a quick meal, most consumers evaluate the price relative to the quality of the product and the value they expect to receive in return. The evaluation of investment products should be no different.

The lowest-cost mutual fund options (which tend to be index-tracking strategies) may exhibit some desirable qualities, such as transparency and broad-based diversification, but index funds typically do not offer the ability to add value over benchmarks. An index-based approach theoretically provides a benchmark return less fees and expenses. These strategies leave potential value on the table, which, over the long term, can have a meaningful impact on plan participants' growth of wealth and their ability to meet their retirement savings goals.

The Employee Retirement Income Security Act of 1974 (ERISA), as amended, also does not stipulate or imply that the lowest-cost option is the best or most prudent. It provides guidance that plan fiduciaries should make diligent and well-supported decisions in selecting investment options. According to the US Department of Labor, fees and expenses are one of several factors to consider when selecting and monitoring plan investments. The level and quality of service and investment risk and return also have an effect on investment decisions.

Evaluating Fund Options for Value to Participants

A value-adding investment approach can still be achieved while charging low management fees and preserving high levels of diversification and transparency. A few considerations beyond fees can be useful in evaluating fund options for these qualities:

Is there a sensible basis?

Many managers claim to have market-beating strategies, but the realized results don't always match the backtest. Data mining, or spurious results, is often the issue. An approach that is sensible and grounded in economic theory, in addition to being supported by robust historical results, can provide greater confidence that higher expected returns will be realized into the future.

Is the implementation efficient?

A portfolio's expense ratio does not represent all costs incurred by investors. Trading costs, in particular, can be significant for some strategies and have a large impact on performance. Efficient implementation is critical if these costs are to be minimized. Achieving this goal starts with designing portfolios to target higher expected returns while keeping turnover low. Strategies that require high turnover may offset any expected premium due to the costs associated with frequent trading.

Flexibility in execution is also important. Strategies that demand immediacy, either to avoid information leakage on a new idea or minimize tracking error against a benchmark, can impact the price and add hard-to-see costs that eat away at returns.

Is the process repeatable?

Any fund may perform well over a given period, but it's important to assess whether such performance results from a repeatable approach or is simply due to short-term luck. Evidence of traditional active managers' difficulty in covering management fees also suggests that strategies seeking to outguess market prices rarely deliver consistent value through time.¹ A transparent and systematic approach to pursuing higher expected returns that has been tested over time and across markets may provide a greater likelihood of outperformance over the long term.

Has the manager delivered on its promises?

Evaluating a manager on what they say they will do goes beyond performance. It's also about trust. Plan sponsors need to trust that managers in their lineup will adhere to their stated approach and objectives and, ultimately, that they are good stewards of participants' capital. Managers should be able to show they have delivered the intended exposures and clearly demonstrate how this approach has contributed to performance—either good or bad. This kind of information is an important input when trying to understand whether plans are getting what they paid for and whether it's worth the cost.

A Track Record of Delivering Value

For more than 35 years, Dimensional has managed investment solutions designed to systematically target securities with higher expected returns and add value over benchmarks. We believe it is sensible to expect differences in expected returns among stocks and look to information in market prices and company fundamentals to identify those differences. We use this information to emphasize securities with higher expected returns in our strategies—those with smaller market capitalizations, lower relative prices, and higher profitability—while maintaining broad diversification and being mindful of implementation costs. This approach has led to long-term, value-added results throughout markets around the world. ◀

For more details on our track record—including trailing 15-year performance after fees of Dimensional funds relative to Morningstar categories—please see is.gd/DFATrackRecord.

Editor's note: A longer version of this article will be available in the next Dimensional DC Quarterly Review email newsletter.

**Considerations
for selecting
and monitoring
investment options:
sensible basis,
cost-effective
implementation,
repeatable
process, and
demonstrated results.**

1. See, for example: Fama, Eugene F. and Kenneth R. French. 2010. "Luck vs. Skill in the Cross-Section of Mutual Fund Returns." *The Journal of Finance*, 65(5), 1915–1947. Eugene Fama and Ken French are members of the Board of Directors of the general partner of, and provide consulting services to, Dimensional Fund Advisors LP.

ADVISOR FOCUS



ANTOINETTE SCHOAR is the Michael M. Koerner (1949) Professor of Entrepreneurial Finance at the MIT Sloan School of Management. Her research interests span from entrepreneurship and financing of small businesses in emerging markets to household finance and intermediation in retail financial markets. She has received several awards, including the Kauffman Prize Medal for Distinguished Research in Entrepreneurship and the Brattle Prize for best paper in the *Journal of Finance*. She also is the cofounder of ideas42, a nonprofit organization that uses insights from behavioral economics and psychology to solve social problems. Schoar holds a PhD in economics from the University of Chicago.

We talked with her about the value of being a fiduciary in the financial advisory arena.

Do Investors Get High-Quality Advice?

Research suggests clients often don't understand incentives shaping behavior of advisors and brokers

► By **Ashish Shrestha**, Head of Advisor Defined Contribution and Vice President
Dimensional Fund Advisors

Do you see differences in the quality of advice delivered by fiduciary and non-fiduciary advisors?

ANTOINETTE SCHOAR: The current structure of the market for financial advice exposes investors to a wide array of different service providers. My research¹ suggests that advisors who have fiduciary responsibility toward their clients provided less biased advice than those who are merely registered as brokers. The former were more likely to educate consumers about the erroneous beliefs they might hold about the market—return chasing behavior, for example. They were also less likely to encourage these types of erroneous beliefs. In addition, we found that registered investment advisors were less likely to guide people toward high-fee funds and away from index funds. However, brokers—advisors not acting as a fiduciary—encouraged return chasing and pushed hard against investment in low-cost index funds.

How do you gauge the quality of advice provided to investors?

SCHOAR: I conducted an audit study, together with co-authors Sendhil Mullainathan and Markus Noeth, looking at the advice that goes into the investment decision. We sought answers to these questions:

1. Do brokers and advisors differ in how they correct well-documented biases (or investment mistakes) that retail customers hold?
2. Do they differ in how they direct clients toward low-fee investment alternatives such as index funds rather than focusing on high-fee options?
3. Do they provide specific customized recommendations based on the needs of the clients?

The answers showed that there are big differences. We sent professionally trained “mystery shoppers” to make more than 250 advisor and broker visits in the greater Boston/Cambridge area of Massachusetts to seek advice on how to invest their retirement savings. We replicated the study with 450 visits in the New York City area. We also varied the shoppers’ levels of bias or misinformation about financial markets to see whether advisors correct these misconceptions.

For example, in half of the visits, mystery shoppers expressed a desire to chase past returns and other well-documented biases that have been shown to have poor returns. Other mystery shoppers went into the advice situation with what you might call a textbook portfolio: well-diversified, low-cost index funds.

What role do incentives play in the quality of advice delivered to investors?

SCHOAR: A large body of literature² shows that conflicted advice is bad for consumers because it pits the interest of the broker against that of the customer, rather than aligning them. When brokers are paid on commission for placing customers into specific investment products, their interest is to maximize these commissions, rather than to maximize the performance of the customer's portfolio. These problems are aggravated if consumers are not aware of or if they do not understand the nature of the conflict of interest that brokers face. My research suggests that customers often do not understand the differences in incentives that advisors or brokers face and the important role that these incentives play in shaping the behavior of the agents they deal with.

Can the value of a fiduciary advisor be quantified?

SCHOAR: I believe that there are several ways in which fiduciary advisors provide value to their clients. First, knowing that your advisor's incentives are well aligned with your own is an important prerequisite in establishing trust between advisor and client. A number of studies³ document that financial markets in which customers have trust in the financial professionals they deal with show larger market participation and more willingness among clients to delegate investment choices. In other words, trust is the basis of well-functioning markets. While this might be the least quantifiable dimension, it might be one of the most important.

Second, our research shows that fiduciary advisors saved their clients significant costs by directing them toward lower-fee funds and more passive strategies, while high fees charged by non-fiduciary advisors were not offset by better performance. Therefore, these fees are just a loss to customers.

“Any policy that reduces conflicts of interest between clients and their advisors helps to harness the market’s competitive forces to the benefit of consumers.”

Antoinette Schoar

Finally, we also found that fiduciary advisors provided their clients with better financial education and a broader picture of all their investment choices, rather than directing them predominantly to mutual funds that provide the most fees to the advisor.

Do you think end-investors can discern a non-fiduciary advisor from a fiduciary advisor?

SCHOAR: Unfortunately, only a small subset of US retail investors seems to be informed enough about the market for financial advice to differentiate between advisors and brokers. In an ongoing study that I am conducting with employees from a number of Boston-based companies, we found that less than 30% of employees were able to determine the registration status of a financial professional when presented with different options. Often, these employees even failed to understand that there was a difference among these choices.

Similarly, most participants in the study did not differentiate between financial professionals based on the compensation structures that they use to charge clients.

What metrics do retail investors use to assess the quality of their advisors?

SCHOAR: We found stark differences between people who are financially more sophisticated and those who are not. The former group looks for advisors with good alignment of incentives and judges the advisor based on the quality of the actual advice. The latter group lacks the knowledge to assess the quality of advice and seems to look for softer metrics, such as whether the advisor was friendly and empathetic or treated them respectfully. Unfortunately, they did not respond to the actual quality of the advice.

How can the industry promote better investment decision-making among end-investors?

SCHOAR: Any policy that reduces conflicts of interest between clients and their advisors helps to harness the market's competitive forces to the benefit of consumers. Therefore, improving the fiduciary standards for financial advisors is a good middle path. It preserves the flexibility of the industry to decide how to organize the provision of advice but still ensures that advisors are acting in the interest of their clients. One important caveat: Investing in financial markets is always risky, so fiduciary standards should be imposed on the soundness of the advice going in. But they should not open up financial advice firms to frivolous lawsuits just because the market went down and a client experienced any losses. ◀

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JOHN D. CALAWAY, Senior Gift Planning Officer at the University of San Francisco since 2014, has 25 years of experience helping hundreds of donors plan their largest gifts to charity. He specializes in testamentary provisions from wills, trusts, and retirement plans, and gifts of non-cash assets. Calaway was formerly the Deputy Chief Advancement Officer of the conservation organization Sierra Club. He has a BA in German from the University of Wisconsin-Madison.

We spoke with Calaway about the impact of the Tax Cuts and Jobs Act of 2017 on estate planning.

Using a DC Plan as a Bequest

New law impacts gifting strategies and estate tax considerations

► By **David Campbell**, Vice President
Dimensional Fund Advisors

With the passage of the Tax Cuts and Jobs Act of 2017, are there new considerations for how we think about our legacy and benefits for our heirs?

JOHN D. CALAWAY: The chief motivation for donors making testamentary gifts to charity hasn't changed—namely, a strong desire to support an institution's mission. Under the previous law, the federal estate tax credit sheltered \$5.6 million of assets transferred to one's heirs at death. Under the new law, the shelter was doubled to \$11.2 million per individual, with married couples now able to shelter estates of up to \$22.4 million. The tax rate on excess amounts remains at 40%.

That said, the new law creates an uncertainty factor: Provided that the law is not changed in the meantime, after 2025, the amount sheltered from estate taxes will revert to \$5 million (\$10 million for married couples), with inflation adjustments factoring back to 2011.

Keep in mind that usually only the very wealthy have taxable estates. In 2013, only 4,700 estate tax returns reported a tax liability out of 2.6 million total deaths in the US, which represented roughly 0.2% of all estates that year.¹

Donors who have taxable estates can reduce their estate tax liability through gifts to charity.

Can you explain why heirs can benefit from a planned gift to charity?

CALAWAY: Twenty years ago, the federal estate tax credit sheltered \$600,000 of assets transferred at death, with excess amounts taxed at 55%. Estate taxes applied to a broader swath of households compared to today. Under the current tax policy, if there's little or no philanthropic motivation, it's difficult to pencil out financial benefits to one's heirs arising from a charitable estate gift.

For qualified plan owners who are philanthropic, generally the smart move is to satisfy testamentary gifts to charity from qualified plans while reserving after-tax assets for their families and other named individuals.

For example, let's say a qualified plan owner intends to bequeath \$100,000 to her nephew and \$100,000 to her alma mater. If she names her nephew as the beneficiary of a \$100,000 IRA and provides a bequest to her university from her living trust, her nephew's bequest will be reduced by a tax liability ranging as high as 37%. But if she names her university as the IRA beneficiary and provides for her nephew using after-tax assets from her living trust, each will receive the full \$100,000.

We try to flag the income tax planning consideration when speaking with prospective donors or their advisors when they are drafting their plans.

Planning a testamentary gift via the beneficiary designation form can be an easy, flexible way to reserve after-tax assets for your family and earmark pretax assets to fulfill your intended gifts to charity.

Are there gift strategies that may lessen the income tax burden while we are still with our loved ones?

CALAWAY: Tax-smart ways to give include:

- Giving long-term appreciated property, such as marketable securities, unencumbered real estate, or closely held business interests. Your gift will not be subject to capital gains taxes, and you'll qualify for a charitable income tax deduction equal to the fair market value of your gift.
- Making annual gifts to charity from your IRA if you are a qualified plan owner aged 70½ and older. When properly carried out, a qualified charitable distribution from your IRA counts toward your required minimum distribution.
- Looking to your qualified plans to fulfill your testamentary gifts to charities (if you are philanthropically minded) and reserving after-tax assets for your family and other named individuals. Charities are not subject to income tax withholding.

Successful savers may not spend the balance of their retirement accounts. Are there special circumstances regarding double taxation and solutions to lessen the tax impact to heirs?

CALAWAY: The double-tax problem refers to the combination of income and estate tax liabilities faced by individuals whose estates are in excess of \$11.2 million (or \$22.4 million for married couples). Typical planning solutions for those who are charitably minded include:

- Passing assets to younger heirs via a charitable lead trust. Under this plan, a donor transfers assets to a trust that provides annual gifts to charity for a specified time, after which the remaining trust assets are distributed to his or her heirs. The donor receives a substantial reduction in transfer taxes in recognition of the annual gifts to charity over the lifetime of the charitable lead trust.
- Creating an income stream for one or more heirs, rather than providing a lump-sum inheritance. The income stream terminates when each heir dies, with remaining funds distributed to charity. Again, the donor can reduce his or her transfer taxes in recognition of the future gift to charity.
- Bequeathing \$1 million to charity from the donor's estate will provide \$400,000 in estate tax relief. If the bequest is fulfilled from a qualified plan asset, the donor also avoids income tax on the \$1 million. The combined income and estate tax relief from testamentary gifts can provide tremendous tax savings for high-net-worth individuals and families who opt to give to charity as a component of their wealth transfer plans.

Most people are required to begin taking retirement distributions at age 70½. Are there planned giving strategies that may lessen their tax liability?

CALAWAY: Yes, annual gifts to charity in the form of qualified charitable distributions. When properly executed, your gifts count towards your required minimum distributions. Under the current tax regulations, you are not permitted to make tax-free transfers of IRA assets to charity in exchange for life income. If you plan to make a bequest to charity, and you have substantial holdings in an IRA, consider giving the maximum of \$100,000 per year.

“Planning a testamentary gift via the beneficiary designation form can be an easy, flexible way to reserve after-tax assets for your family and earmark pretax assets to fulfill your intended gifts to charity.”

John D. Calaway

Are there any potential stumbling blocks when providing a retirement asset as a gift to charity?

CALAWAY: There are several downsides:

- The provision doesn't allow you to specify the gift's purpose or a pecuniary gift (dollar amount), if that's important to you.
- The provision is easily revoked when assets are transferred from plan to plan or consolidated.
- Your provision is nullified if you've drawn down the account at death. Your will or living trust must be carefully drafted to authorize your personal representative to fulfill charitable provisions using pretax assets where possible. ◀

1. "History, Present Law, and Analysis of the Federal Wealth Transfer Tax System." March 2015. The Joint Committee on Taxation. jct.gov/publications.html?func=startdown&id=4744.

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PROVIDER SPOTLIGHT



PETE KIRTLAND, CEO, oversees the growth and strategic direction of Aspire, a nationally recognized leader in the retirement plan industry. He has led Aspire to represent the new age of retirement planning, operating in the best interests of clients through transparency and a fixed-fee cost structure to promote advocacy for participants and flexibility with investment choices. Kirtland has spent over 28 years in the industry, serving in several senior roles of large global professional services companies and entrepreneurial positions leading to startup success.

We talked with Kirtland to get his insights on advisors operating in the small-plan market.

Uncovering Opportunity in the Small-Plan Market

Aspire explains how advisors can thrive by offering scalable solutions

► By **Brian W. Dannemann**, Regional Director
Dimensional Fund Advisors

Many advisors have avoided the small-plan market, stating it's too hard to make money. What has changed?

PETE KIRTLAND: First and foremost, the competition is fierce up market, where it's often a race to the bottom on fees. The fee compression has been amazing. I had one advisor tell me he won a \$50 million plan but had to come down to 9 basis points (bps)¹ in fees to win it. Comparatively speaking, it's not uncommon to see advisors charging 50–100 bps in the small-plan market. In addition, the business can be much easier to win. You can have an initial meeting with a business owner who could become a client that afternoon. And these clients can be clients for life. Contrast that to completing a request for proposal (RFP), finals presentations, and approvals by large committees.

Also, advancements in the industry now allow you to use low-cost, institutional share class investments

in the smallest of plans, even SIMPLE IRAs. In addition, you may not have to worry about the plan going out to an RFP process every three years.

What is the key to an advisor making a small-market solution successful and profitable?

KIRTLAND: First, cost of acquisition needs to be low. We have seen great success when advisory firms get connected to centers of influence, such as CPA firms, chambers of commerce, or other associations. Second, the solution needs to be scalable. This means you have a consistent, repeatable process. We are seeing a lot of different iterations of plan aggregation solutions. These solutions are similar to a multiple employer plan (MEP) in that each plan effectively has the same provisions, same fund lineup, etc. And, if you use models, they should be managed at a global level. To the extent possible, you may want to avoid “uniqueness” between plans that use your model, as this

may challenge scalability down the road. Third, the plan onboarding needs to be a somewhat automated process, even leveraging online capabilities, if available, to speed up the process.

Do you consider this trend to be lasting, and if so, why?

KIRTLAND: We suspect this trend will likely last for some time. Small employers are the backbone of the American economy. In fact, 140,000 net new small businesses (less than 100 employees) were started between 2012 and 2014.² [See *Exhibit 1 for data on retirement plan usage by small businesses.*] Additionally, workforce demographics are shifting considerably. More and more workers are becoming independent contractors, also known as gig workers, which will affect how they are able to save for retirement. We are beginning to see the use of Payroll Deduction IRA programs becoming much more prevalent.

Exhibit 1 Access and Participation in Retirement Plans

As of March 2017

Private firms with 1-99 workers



Private firms with 100+ workers



Source: Bureau of Labor Statistics, National Compensation Survey: [bls.gov/news.release/pdf/ebs2.pdf](https://www.bls.gov/news.release/pdf/ebs2.pdf).

Are you seeing the emergence of any new or different solutions to support this market space?

KIRTLAND: One interesting concept to emerge is what we refer to as the Retirement Savings Continuum. This simply suggests starting a small employer with a Payroll Deduction IRA or SIMPLE IRA and, as the company grows, putting in a 401(k) using the same investment lineup and same recordkeeping platform. Simultaneously, we establish an omnibus IRA with the same investment lineup and recordkeeping platform, allowing you to move employees who have separated from service into this IRA solution. This approach allows the advisor to forge a lifetime relationship with each employee.

How do you see this concept benefitting the participant?

KIRTLAND: Inertia tends to be one of the biggest obstacles when trying to get employees to save for retirement. The Retirement Savings Continuum concept creates a paradigm in which the participant experiences continuity in the act of saving, just in different plan constructs, avoiding the resistance created by learning new technology and new investments. Let's face it: Most people resist change of any kind. And to be able to use low-cost, institutional share class funds with plans of this size makes this solution even more compelling. We have already seen positive effects using this approach and are optimistic about the impact it can have in helping to achieve optimal retirement outcomes while helping advisors grow their practice. ◀

Advisors who want to learn more about small-market opportunities can visit retirementsavingscontinuum.com.

“To the extent possible, we believe you should avoid ‘uniqueness’ between plans, as this will challenge scalability down the road.”

Pete Kirtland

1. A basis point is equal to 0.01%.

2. US Small Business Administration, Office of Advocacy, from data provided by the US Census Bureau, Business Dynamics Statistics.



IAN KOPELMAN has extensive experience in ERISA and is responsible for all matters involving retirement and other fringe benefit programs for clients ranging in size from major publicly held corporations and public benefit plans to sole proprietorships and partnerships.

Fiduciary Considerations for Employers Offering HSAs

It's important to understand the advantages—and possible trouble spots

► By **Ian Kopelman**, Partner
DLA Piper

Health Savings Accounts (HSAs) have become increasingly popular since they were created legislatively in 2003, with assets totaling a reported \$45.2 billion at the end of 2017.¹ While these accounts need not be tied to employment, many employers offering group health plans now offer HSA accounts to help employees pay for medical expenses not covered by High Deductible Health Plans (HDHPs). Available only to employees with no health insurance other than a HDHP, these individually owned, fully vested bank accounts also allow tax-favored funds to accumulate over many years, making HSAs attractive long-term savings vehicles.

Given these basic attributes, two overarching fiduciary considerations arise:

1. By attending to minimal guidelines, an employer can offer these accounts without establishing an ERISA plan and reduce the compliance obligation and concurrent risk of compliance failures.

2. Even if ERISA does not apply, the employer remains subject to the prohibited transaction rules of the Internal Revenue Code and would be wise to incorporate an ERISA standard of care in operating the program, including selection and monitoring of the provider and investment opportunities for employees.

Offering HSAs without ERISA: Why That May Matter

If the HSA program is not treated as an ERISA plan, the employer is not an ERISA fiduciary and thus not held to the exacting ERISA prudence and loyalty duties.² Further, compliance obligations are significantly reduced. The employer need not file Form 5500, prepare a plan document, provide a summary plan description, adopt a claims procedure, offer COBRA coverage, or comply with HIPAA portability or nondiscrimination rules. Neither does a dispute become a federal case.

Establishing and Maintaining Non-ERISA Plan Status

The US Department of Labor (the federal agency with ERISA regulatory and enforcement authority) has stated that HSAs generally will not constitute employee welfare benefit plans (ERISA plans) if employer involvement with the HSA is limited—even though the accounts may be associated with an HDHP, which will almost certainly be an ERISA plan. The DOL has published guidance that is helpful in defining that limited involvement.³ These guidelines essentially require the following:

1. The employer may not:
 - Limit the ability of employees to roll their funds over to a different HSA (beyond Code restrictions).
 - Impose conditions on using funds. This would include communicating that HSA distributions can only be used for medical expenses.

- Make or influence investment decisions.
 - Represent that the HSAs are an employee welfare benefit plan established or maintained by the employer. Information about the HSA program will likely be communicated with details about other programs that definitely are ERISA plans. So language is crucial in distinguishing the HSAs. An explicit statement that the HSA program is not subject to ERISA is also suggested.
 - Receive any payment or compensation in connection with the HSA, including a discount on another product from the vendor. The DOL explains, though, that contributions could be made through a cafeteria plan, and the resulting employer savings in FICA and FUTA taxes would not constitute such “payment or compensation.”
2. The employer may:
- Limit the HSA providers it allows to market products in the workplace or select a single provider to which it will forward contributions through its payroll system.
 - Select an HSA carrier that offers limited investment options or options that replicate those in the employer’s 401(k) plan.
 - Contribute to the HSA or pay fees that employees would otherwise be required to pay.
 - Provide general information on the advisability of using an HSA in conjunction with the HDHP.
3. Finally, the employee’s decision to contribute, through salary reduction or otherwise, must be

completely voluntary. (As to employer contributions, the employer could establish accounts and contribute without employee consent and still not negate this voluntary requirement.)⁴

No Avoiding Internal Revenue Code

The Internal Revenue Code, like ERISA, prohibits specified transactions considered conflicts of interest, and these prohibited transaction rules explicitly apply to HSAs. An employer could carefully maintain a non-ERISA program and still run afoul of these rules, which carry excise taxes. In the HSA context, a likely trouble spot is the transmission of employee contributions. A failure to transmit these contributions promptly to the HSA trustee or custodian will violate the prohibited transactions rules.

Some Form of Due Care Is Required

In addition to the Code’s prohibited transaction provisions, a non-ERISA HSA program is subject to state laws. That brings up ERISA preemption. ERISA preempts state law dealing with ERISA-covered employee benefit plans. Without the uniformity of ERISA, an employer’s operation of its HSA program can be subject to any number of different state laws, such as codified trust or fiduciary law or the common law of trusts; an employee claim could be based on contract law or negligence.

It’s wise to assume that decisions affecting employee funds must be made with care. For example, a Wisconsin court of appeals grafted an ERISA-like standard of care onto the administration of a non-ERISA 403(b) plan, finding the school district would be liable for losses “if it failed to use the degree of care, skill, and judgment that reasonably prudent administrators would exercise under like

or similar circumstances.”⁵ As such, an employer would be well served by treating the HSA program with no less care than its ERISA plans. Using and documenting a responsible process for choosing and monitoring a provider gives the employer a defensible position.

Factors for consideration include:

1. Review and compare fees. Fees may be charged for account opening, account maintenance, specific transactions, etc., that vary widely among vendors. Insist that fees be clearly stated.
2. Whether the vendor provides investment options or self-directed accounts. (The DOL has stated that a single investment option is not reasonable.)
3. If investment options are offered, rather than a self-directed account, understand the options, how they were selected, their relative expenses, their share class, and the adequacy of the array.
4. Know who earns revenue on the investments and in what amount.
5. Understand how and where funds will be held. If the provider is not a bank, how does it select banks or insurance companies to place funds? Are funds FDIC-insured? Are they held in separate accounts or commingled?
6. Review qualifications and employee satisfaction data.

In short, employers can limit their compliance obligations when setting up HSAs that help their HDHP-covered employees achieve tax-favored health care payment and savings goals. But employers must be careful how they go about it. ◀

1. 2017 Year-End Devenir HSA Research Report, devenir.com/research/2017-year-end-devenir-hsa-research-report/.

2. If an HSA program is an ERISA plan, the extent to which the employer is consequently a fiduciary depends on the employer’s stated and functional roles. That is, the employer is a fiduciary if named in plan documents as the administrator or named fiduciary or if it functions as a fiduciary by, for example, selecting the HSA provider.

3. Field Assistance Bulletin No. 2004-01, dol.gov/agencies/ebsa/employers-and-advisers/guidance/field-assistance-bulletins/2004-01.
Field Assistance Bulletin No. 2006-02, dol.gov/agencies/ebsa/employers-and-advisers/guidance/field-assistance-bulletins/2006-02.

4. In addition to these guidelines, an employer that does not intend to contribute to employee HSAs could avoid ERISA plan status by conforming to the group-type insurance program safe harbor set out in DOL regulation 29 C.F.R. 2510.3—1(j), in which the program is voluntary and not contributed to or endorsed by the employer.

5. *Ann Catteau v. Natl. Insurance Services of Wisconsin, Inc. et al.*, 2015 WI APP 40 (Ct. App. Wisc.2015).



ZVI BODIE, Professor Emeritus of finance at Boston University, holds a PhD from the Massachusetts Institute of Technology and is a coauthor, with Alex Kane and Alan Marcus, of the widely used textbook *Investments*. Bodie also co-wrote the textbook *Financial Economics* with Nobel laureate Robert C. Merton, Resident Scientist at Dimensional Holdings Inc., and David Cleeton. A revised edition of *Worry-Free Investing*, coauthored by Bodie and Michael Clowes and originally published in 2003, will be released soon.

We last spoke with Bodie, a key industry thought leader, on the heels of the 2008 Boston University-sponsored "Future of Life-Cycle Saving and Investing Conference." In this follow-up conversation, we get Bodie's thoughts on the latest trends in America's employer-sponsored (private) retirement system.

Connecting DC Plans and Financial Wellness

Dr. Zvi Bodie discusses role of employers in improving financial health of plan participants

► By **Aaron Borders**, Regional Director and Vice President
Dimensional Fund Advisors

Please tell us about why you are planning to publish a revised edition of *Worry-Free Investing*.

ZVI BODIE: The risks facing retirement plan savers, and thus the private retirement system, have not changed much since 2008. In the revised edition, I plan to expand the section on retirement and devote a standalone section to worry-free investing just for retirement. The examples will be redone to reflect today's lower interest rates. Also, since the original edition was published, several individuals have built websites that implement the strategies described in the book. I will provide links to websites that I endorse in the revised edition. I also intend to provide a companion website with videos like those posted on my YouTube page. These videos were produced in 2008 for employees of Boston University.

Today, financial wellness seems to be in the news. What impact will that have on retirement savings and/or DC plans?

BODIE: I am glad to see the conversation being elevated to one that looks at the comprehensive financial wellness of plan participants. Having a feasible retirement plan is a fundamental feature of financial wellness. Defined contribution (DC) plans play an increasingly important role in overall financial wellness and will need to deliver on the promise of providing sustainable retirement income.

That is why it is so critical that we orient DC plans and participants toward the goal of income in retirement and address the risks associated with this goal. [See related article on page 24.]

Do you think employers can or should play a vital role in fostering financial wellness?

BODIE: This is really a question of access and trust. Who can employees trust to provide them with good financial advice at a reasonable cost? The reality is that many private-sector employees do not have a relationship with a personal financial advisor, and their company retirement plan may be their primary source of savings. Then, at the point they need financial advice most, they need to be assured they are receiving trustworthy service. So I strongly believe that employers can (and should) provide guidance and advice to their employees that will help improve their financial wellness.

The employer's interests regarding financial wellness should be aligned with those of their

employees, and employees typically have confidence that the benefits office (HR department) is on their side. It makes sense that employers would want their employees to feel secure. Financial wellness—and physical wellness, too—can play a big part in that initiative.

How do you see technology innovations potentially improving individual financial wellness?

BODIE: Technology, such as robo-advice, can make guidance more accessible and affordable for many people. It is important, however, that we don't lose sight of the old adage of garbage in, garbage out. Advances in technology and access are not necessarily the same as good advice. Some conventional advice about investing is misleading and downright wrong. No matter how advanced the technology, I believe that there is no substitute for a trusted human advisor who can help clients apply that technology to their own circumstances and overcome the procrastination that can pervade personal financial planning.

What do you see as the greatest financial risk facing the global economy as a result of aging populations and increasing longevity?

BODIE: In my view, the greatest risk is that the burden of providing income for people retiring from the labor force will fall on a shrinking labor force. It's already happening and should be a major wake-up call for policy makers. The problem is most evident in those countries with pay-as-you-go retirement systems. The contribution rate

needed to maintain balance can become unreasonably high and is unsustainable in the long run. In cities and states with underfunded public pension plans, tax rates will likely need to be raised to unacceptable levels to support the system moving forward. That's why the private retirement system is so important and why we must get the design of these systems right. Expanding coverage in the private retirement system and helping people to achieve the goal of a sustainable level of consumption in retirement will have a big impact on productivity and the global economy.

What is the biggest issue policy makers should attempt to address from a legislative or regulatory perspective?

BODIE: In the US, I see two major threats. The first is the increasing burden on taxpayers from underfunded public pension liabilities. The second is the lack of knowledge about the risks facing participants in the private retirement system and flawed safe-harbor rules for qualified default investment alternatives. I believe both threats have the potential to create a financial crisis. I worry that participants who have target date funds in DC plans may be under the false impression that they have a government guarantee of sufficient assets at retirement that can maintain their preretirement standard of living. No such guarantee exists. The good news is that policy makers can address both issues. The key criterion for a better retirement savings framework involves targeting the right goal for retirees, which, for most, is enough income to sustain their essential standard of living for as long as they live. ◀

“Having a feasible retirement plan is a fundamental feature of financial wellness. DC plans play an increasingly important role ... and will need to deliver on the promise of providing sustainable retirement income.”

Zvi Bodie

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Dimensional Fund Advisors LP receives compensation in the form of investment management fees from investments made by Boston University. Robert Merton provides consulting services to Dimensional Fund Advisors LP. Zvi Bodie is an occasional speaker at Dimensional Fund Advisors LP events and receives honorarium for his services.



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Financial Wellness

Key answers for plan sponsors

► By **Tony Verheyen**, **Brandon Diersch**, and **Tim Kohn**

Tony Verheyen, former Executive Director of the Plan Sponsor Council of America; Brandon Diersch, Group Portfolio Manager for Capital Markets at Microsoft; and Tim Kohn, Head of Defined Contribution Services at Dimensional Fund Advisors, recently co-authored articles in the *Journal of Pension Planning & Compliance* and *Defined Contribution Insights* that outlined key considerations for workplace financial wellness initiatives. Here, they offer a detailed summary for plan sponsors.

Given the nation's tight labor market, increasingly diverse workforce, and strong interest in financial health (see **chart**, page 25), many plan sponsors are eager to implement cost-effective programs that improve employee saving, borrowing, and investing while protecting retirement readiness. What follows are seven questions and answers that plan sponsors should consider when assessing these initiatives.

What is the goal?

Generally, organizational needs to compete for labor, impact employee behavior, create a sense of internal fairness, and optimize cost and tax efficiencies drive the design of employee benefit plans. While financial wellness initiatives can be understood in that context, plan sponsors

seem to believe that such programs can help organizations achieve three tangible goals:

- **Reduce human capital expenditures.** Plan sponsors increasingly believe that they will spend less on benefits if employees embrace healthy financial behaviors. While this correlation is difficult to demonstrate empirically, advocates for wellness programs argue that reduced financial stress can result in reduced systemic physical and mental illness, which can lower health care costs.
- **Improve plan participation and utilization.** Many plan sponsors believe financial wellness initiatives will help to increase participation in their core benefit programs, in addition to boosting utilization and appreciation.

Employee Interest in Financial Health

Continued uncertainty about the future is causing employees to look for greater security.

My retirement security has become a more important issue for me over the last two or three years

78%

Managing my finances is a top priority in my life

69%

Managing my health is a top priority in my life

65%

- **Increase engagement and satisfaction.** As organizations look to improve employee engagement, they focus more on the role that financial stress plays in absenteeism, presenteeism, productivity, and turnover.

Who is the audience?

Many plan sponsors believe holistic financial wellness can help their entire workforce. The reality is that some groups of employees may dismiss organizational efforts in this space. Why? Some individuals already embrace financial wellness on their own. Others may never embrace the behaviors, habits, decisions, and actions promoted by the program. As such, plan sponsors should clearly identify those employees who are most likely to both adopt a “healthy” mindset and take advantage of the program (How do employees feel about financial wellness programs? See **Exhibit 1**, below).

What is the scope?

For plan sponsors thinking about adopting or enhancing a financial wellness program (see **Exhibit 2**, page 27), there are three ways to characterize and narrow the scope of their efforts.

- **Integrated or siloed.** Integrated initiatives are closely connected with other benefit plans, wellness initiatives, life skill initiatives, and personal financial programs (e.g., emergency savings, basic budgeting, consumer debt). Siloed initiatives promote or rely on standalone solutions (e.g., personal financial mobile apps, debt, and retirement planning).
- **Comprehensive or limited.** Comprehensive programs address a wide range of employee needs, including saving, spending, borrowing, investing, health planning, estate planning, etc. Organizations seeking to tie together health, mental, and financial wellness needs for their workforce may prefer such programs. Limited-scope programs address the unique needs of a specific group of workers or workforce challenges, such as HSA-401(k) optimization.

- **Consultative or transactional.** Consultative programs attempt to facilitate improvements in employees’ financial decision-making by using education, coaching, and counseling. Transactional programs employ quick, easy, and cost-effective solutions for employees’ typical financial challenges. This second approach may eliminate the need for momentum-eroding deliberation and facilitate immediate implementation of solutions.

What are the desired outcomes?

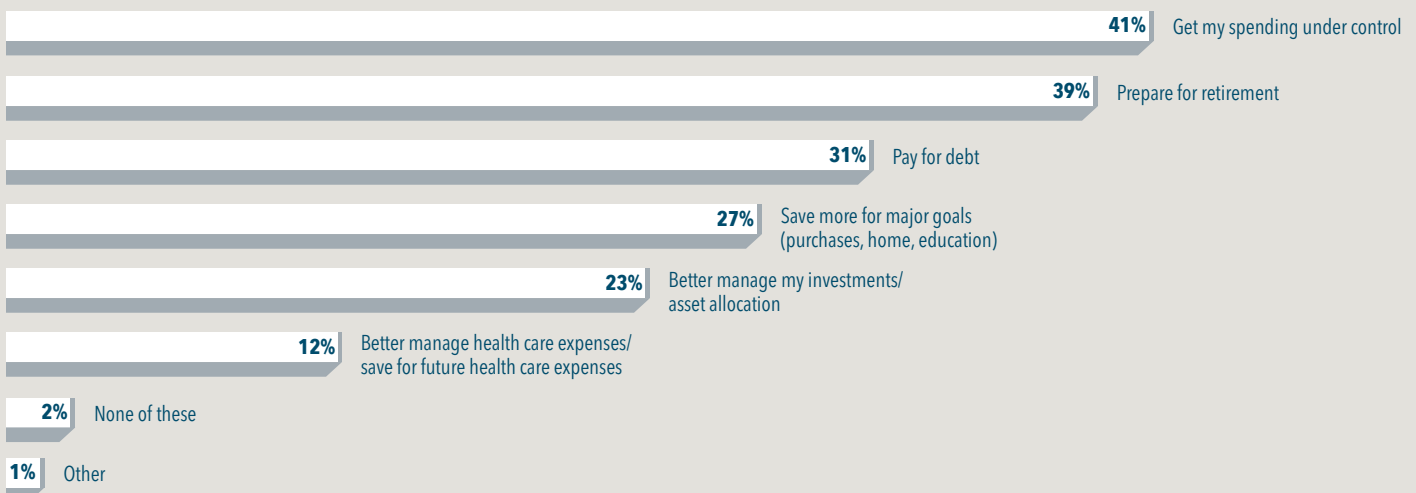
In a formal financial wellness program, plan sponsors should clearly create efficient avenues to new or existing services that result in desirable actions (e.g., call a counselor, contribute to an HSA, purchase identity theft protection, etc.). As desired actions are defined, consider ways to make them less contemplative and more reflexive; behavioral research suggests that the former is more likely to lead to inaction.

What resources are available?

Given the widespread belief that financial stress affects other aspects of organizational well-being, vendors across the benefits spectrum

Exhibit 1 Employee Views on Financial Wellness Programs

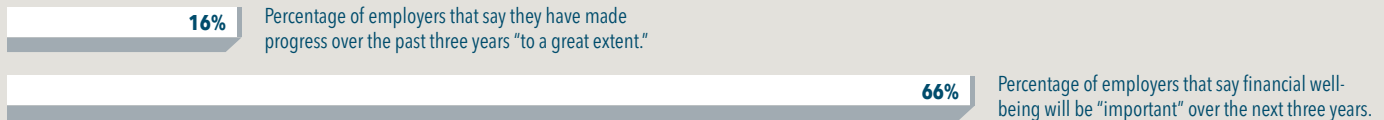
In a 2018 survey,* US workers said their firm’s program helped:



*Employees could choose as many answers as applicable. Source: PwC 2018 Employee Financial Wellness Survey. Incorporates views of 1,600 full-time employed adults in US.

Exhibit 2 Employer Views on Financial Wellness

In a 2017 survey, most employers said they want to implement solutions to improve the financial health of their workforce:



Source: 2017 22nd Annual Willis Towers Watson Best Practices in Health Care Employer Survey, completed by 698 US employers with at least 100 employees between June and July 2017. Reflects respondents' 2017 health program decisions and strategies and expected changes for 2018 and 2019. Respondents collectively employ 11.9 million employees and operate in all major industry sectors. © 2018 Willis Towers Watson. Used with permission.

are attempting to demonstrate their ability to address the problem by offering expanded services, some as value-adds. So it is possible internal and external business partners may be working unilaterally to implement similar financial wellness initiatives:

- **Internal business partners** may include colleagues focused on organizational strategy, human resources, benefits, finance, risk management, payroll, wellness, communications, or training.
- **External business partners** may include current and potential providers, and they should be used to recognize gaps, tap underutilized resources, and identify marketplace best practices.

For the sake of efficiency and consistency, the smart approach is to identify all potentially interested parties, confirm oversight responsibilities, inventory all relevant financial wellness resources, and address real or potential conflicts of interest.

Are there any legal and/or regulatory concerns?

Integrating financial wellness initiatives with health/welfare and retirement plans may raise legal and regulatory compliance issues.

Plan sponsors should not overlook potential fiduciary and legal responsibilities. For example, representatives of the Employee Benefits Security Administration recently explained in public forums that ERISA, HIPAA, ACA, and ADEA compliance could apply to financial wellness initiatives when integrated with health plan incentives. Not only should plan sponsors consider the inherent fiduciary exposure but also the potential harm to participants when hiring vendors with real or potential conflicts of interest.

What is the best way to communicate with employees?

Plan sponsors have an abundance of media options at their disposal. They should identify available communication resources and adopt messages that:

- **Avoid** industry jargon, difficult math, confusing graphics, legalese, disclaimers, and messages that shame, condescend, finger-point, or confuse.
- **Embrace** simple, actionable, and eye-opening messages.
- **Engage** internal teammates who will champion financial wellness in the workplace.
- **Incorporate** a personalized, targeted, and branded approach.

Ultimately, the campaign should underscore the organization's commitment to improving employee financial well-being and match the targeted audience's sophistication and preferences.

All expressions of opinion are subject to change.

Tony Verheyen is an occasional speaker at events sponsored by Dimensional Fund Advisors LP or one of its affiliates and receives honoraria for his services.

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In the News

Dimensional's HSA Program Wins First Place Eddy Award



From left, Sara Caddy, Oliver Rowe, and Aaron Marcus of Dimensional's HR team.

Dimensional and HealthSavings Administrators,¹ a service provider for Dimensional employees, received a first place Eddy Award in the retirement health care savings category at the *Pensions & Investments 2018 East Coast Defined Contribution Conference* in Miami. Since 1995, the Eddy Awards have focused on best practices by plan sponsors and service providers. Thanks to the efforts of its Human Resources team, Dimensional offers unique

small-group educational meetings focused on health savings accounts and has an above-average HSA usage rate and overall participant savings rate. HSAs have long-term potential as a retirement aid because they feature tax-free contributions, tax-deferred earnings, and tax-free distributions for qualified health care expenses.

1. HealthSavings Administrators provides health savings accounts in which Dimensional funds may be selected. Dimensional Fund Advisors LP receives compensation in the form of investment management fees from clients who invest in these funds.

Utah Plan Featuring Dimensional Changes Program Name to "my529"

my529[™] Effective February 5, 2018, the Utah Educational Savings Plan changed its name to my529.² The plan includes 10 Dimensional funds as investment options.

Earnings accumulated in a 529 account are not subject to federal and Utah state income taxes if used for eligible education expenses at institutions in the US or abroad that accept federal financial aid. Neither the account owner nor beneficiary is required to be a Utah resident.³ Morningstar recently gave the Utah plan a "Gold" rating.

2. Dimensional Fund Advisors LP receives compensation in the form of investment management fees from clients who invest in Dimensional Funds recommended or offered by intermediaries such as my529.

3. The state in which you or your beneficiary pays taxes or lives may offer a 529 plan that provides state tax or other benefits, such as financial aid, scholarship funds, and protection from creditors, not otherwise available to you by investing in my529. You should consider such benefits, if any, before investing in my529.

Dimensional's AUM in DC Passes \$60B as of March 2018

Dimensional Fund Advisors' assets under management invested in defined contribution plans advanced past \$60 billion as of March 31, 2018. "Our focus on all ends of the marketplace has allowed us to offer our unique investment approach to DC plans of all sizes," says Tim Kohn, Head of DC Services and Vice President. "That approach is sensible and repeatable, and it consistently demonstrates results."

Lori Lucas Appointed President, CEO of Employee Benefit Research Institute



Lori Lucas, a former Executive Vice President at Callan, was named President and CEO of the Employee Benefit Research Institute (EBRI) in February 2018. Lucas has been involved with EBRI since 1999 and most recently was the Vice Chair. She intends to make the organization's research more widely accessible and relevant to members, the industry, policy makers, the media, and the general public. Lucas, immediate past Chair of the Defined Contribution Institutional Investment Association (DCIIA), is a CFA[®] charterholder and has a master's degree from the University of Illinois and a bachelor's degree from Indiana University.

PSCA Research Paper Presents New Savings Withdrawal Strategies

A new paper from the Plan Sponsor Council of America (PSCA)⁴—"Helping Plan Participants Help Themselves: Withdrawal Strategies in a Self-Serve World"—offers three innovative retirement income strategies, one from an individual perspective and two from an employer-sponsored or institutional perspective. Contributors include Philip Murphy of S&P Dow Jones Indices, Steve Vernon of the Stanford Center on Longevity, and Kevin T. Hanney and Kenneth Levine of United Technologies. The paper is available at pasca.org/withdrawal_strategies_NC2018.⁵

4. Dimensional Founder and Executive Chairman David Booth and Head of DC Services Tim Kohn chair the PSCA Investment Committee. Kohn is also a member of the PSCA Board of Directors.

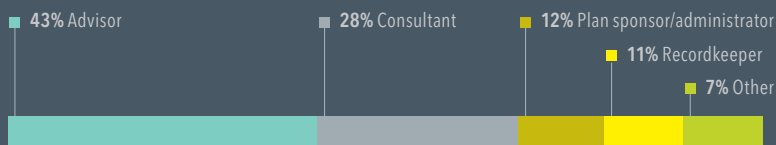
5. The link to the PSCA paper is provided for your convenience and information only. Target date funds are designed to target a year in which an investor may withdraw funds for retirement or other purposes. Investments in target date funds are subject to the risks of their underlying funds, and asset allocations are subject to change over time in accordance with each fund's prospectus. An investment in a retirement income from a target date portfolio is not guaranteed at any time, including on or after the target date. An investment in a target date portfolio does not eliminate the need for investors to decide—before investing and periodically thereafter—whether the portfolio fits their financial situation. Dimensional Fund Advisors LP receives compensation in the form of investment management fees from clients who invest in Dimensional funds recommended or offered by intermediaries such as Prudent Investor Advisors. Prudent Investor Advisors and Dimensional Fund Advisors LP are not affiliates and are separate entities.

Reader Survey

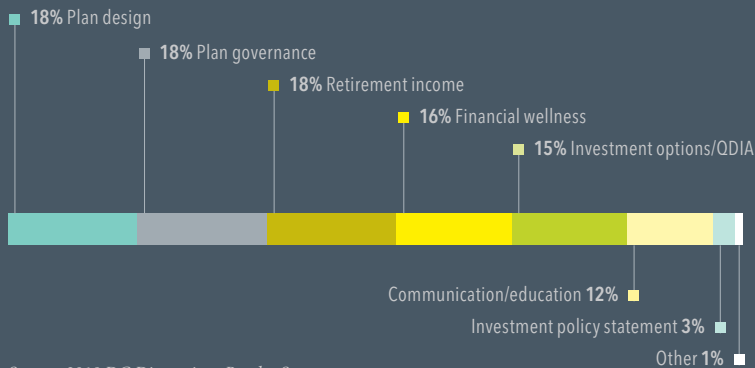
By **Aaron Borders**, Regional Director and Vice President,
Dimensional Fund Advisors

In the first half of 2018, Dimensional surveyed 100 readers of *DC Dimensions* to gauge which issues are top of mind for plan sponsors, consultants, advisors, and recordkeepers. On average, these readers have almost 20 years of experience in the defined contribution industry. Here are some highlights from our findings:

Your role in the DC industry



Most important area of focus for your DC plan(s) in the next year



Source: 2018 DC Dimensions Reader Survey.

Usefulness of hearing from other plan sponsors about their best practices



(1 = not at all important, 7 = extremely important)

Importance of having an income focus* in your DC plan



(1 = not at all important, 7 = extremely important)

*Directing participants to information about how much annual income they can expect from their retirement savings.

Upcoming Events 2018

SEPTEMBER 9-11

LAGUNA NIGUEL, CA
RPAG National Conference

SEPTEMBER 24-26

ORLANDO, FL
529 Annual Conference

SEPTEMBER 25

PHILADELPHIA, PA
Dimensional DC Workshop

OCTOBER 21-23

SAN DIEGO, CA
Pensions & Investments West Coast
Defined Contribution Conference

OCTOBER 25

AUSTIN, TX
Dimensional DC Workshop

NOVEMBER 13-14

SAN FRANCISCO, CA
DCIIA Academic Forum

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