Universal Small Employer Retirement Savings Program

THE SPARK Institute, Inc.

SHAPING AMERICA'S RETIREMENT

About The SPARK Institute

The SPARK Institute represents the interests of a broad based cross section of retirement plan service providers and investment managers, including banks, mutual fund companies, insurance companies, third party administrators and benefits consultants. Our members include most of the largest firms that provide record keeping services to employer-sponsored retirement plans, ranging from one participant programs to plans that cover tens of thousands of employees. Through the combined expertise of our member companies, The SPARK Institute provides research, education, testimony and comments on pending legislative and regulatory issues to members of Congress and relevant government agency officials. Collectively, our members serve over 62 million defined contribution plan participants.

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Contact:
Larry Goldbrum, General Counsel
The SPARK Institute
Larry@sparkinstitute.org
704-987-0533

Introduction

The SPARK Institute developed the Universal Small Employer Retirement Savings Program ("USERSP" or the "Program") concept to create a simplified and standardized savings plan for small employers that have been unwilling to adopt one of the current employer-sponsored plans that are available. The Program will help solve the retirement plan coverage gap for tens of millions of American workers who currently don't have access to employer-sponsored plans. Additionally, the Program is intended to address small employers' concerns (e.g., potential liability and costs)[1] through a plan that service providers can offer and maintain cost effectively.

Part I provides a summary of the features and requirements that should be included in the Program. Part II provides additional information regarding each feature and requirement.

[1] "The Case for Employer-Sponsored Retirement Plans – Coverage, Participation and Retirement Security," The SPARK Institute, May 2009, see pages 6-9.

I. Summary of USERSP

A. **Employer Eligibility** – A USERSP may be offered by any small employer (i.e., less than 100 employees), with at least one non-owner employee. Any employer that offers a USERSP would not be required to offer a mandatory payroll deduction IRA ("auto-IRA") to its employees.

B. **Automatic Plan Features** – Every USERSP must include mandatory enrollment and contribution escalation features with participant opt out.

C. **Contribution Limits** – USERSPs should be subject to lower contribution limits than 401(k) and "SIMPLE" plans, but have higher limits than IRAs so that American workers have reasonable opportunities to save enough for retirement through these plans.

D. **Simplified Plan Documents** – All USERSPs would use the same government approved prototype plan document. The use of a model plan by all service providers and employers would substantially reduce administrative costs and would relieve employers of the enormous and costly burden of ensuring that their plan documents comply with applicable legal requirements.

E. **Limited Plan Features to Prevent Savings Leakage** – USERSPs would have limited plan features to prevent pre-retirement savings leakage (i.e., no loans and limited hardship withdrawals).

F. **Simplified Administration** – USERSPs would not be subject to existing discrimination testing. The elimination of discrimination testing will substantially reduce the compliance administrative burdens. The requirements that all employers offer a plan and that such plans include mandatory enrollment offset the need for such testing by providing access to a plan for all employees and requiring employees to affirmatively opt out if they choose not to save. Moreover, data shows that significant numbers of employers who are unable to make meaningful contribution to their own plan due to discrimination testing failures terminate such plans.

G. **No Mandatory Employer Contributions** – Employers would not be required to make contributions to the plan. However, limited voluntary employer contributions would be permitted.

H. **Simplified Investment Option Selection and Fiduciary Exposure** – USERSP investment options would be required to meet specified minimum requirements for broad based investment choices. Investment options can be chosen by either the employer, if it prefers to do so and the service provider's arrangement allows for it, or determined by the service provider as part of its product offering. Employers and service providers would be protected from potential liability for investment losses for investments that satisfy safe-harbor criteria specified under the Qualified Default Investment Alternative rules for auto-enrollees or as participant directed investments meeting the rules and conditions specified under ERISA Section 404(c).

I. **Multiple Employer Record Keeping Aggregation** – In order to help reduce administrative costs and leverage potential investment option economies of scale among many participating small employers, record keepers should be permitted to aggregate assets across plans and employers, provided that individual plan and participant assets can be separately identified and accounted for.

J. **Consolidated 5500 Reporting** – Service providers should be permitted to submit consolidated annual Form 5500 reporting at the service provider level for the plans they service.

K. **Electronic Communications** – In order to help drive better outcomes and reduce administrative costs, participant communications, whether required or voluntary, should be defaulted to electronic delivery. Participants would always have the option to receive any and all information via hard copy at no charge. Participants also have access to the internet to allow for them to retrieve information.

II. Detailed Discussion of Program Features and Requirements

The following sections provide more information about each feature and requirement, including the reasoning and justification for each, and identify legal and regulatory changes that may be needed to create the Program.

A. **Employer Eligibility** – A USERSP may be offered by any small employer (i.e., less than 100 employees), with at least one non-owner employee. Any employer that offers a USERSP would not be required to offer a mandatory payroll deduction IRA to its employees.

The primary objective of the USERSP is to provide small employers with a robust, simple, and cost effective employer-based retirement savings plan alternative to the plans that are currently available and to the proposed mandatory payroll deduction IRA. The USERSP is designed to address many of the issues and concerns that have prevented employers from otherwise voluntarily adopting the options that are already available. The greater appeal of the USERSP concept should facilitate policy makers' goals of increasing coverage and access to employer-sponsored retirement plans for more working Americans. This USERSP would have to be created through Congressional action and, as discussed more fully below, certain aspects of the concept will require changes to certain existing laws and regulations.

B. Automatic Plan Features – Every USERSP must include mandatory enrollment and contribution escalation features with participant opt out.

Among the issues and concerns that the USERSP addresses are lower participation and contribution rates in small employer plans. The success of automatic enrollment and escalation features is well established and documented. Significant data shows that the vast majority of automatically enrolled employees remain in their employers' plans. The USERSP leverages automatic plan features and makes them mandatory. Employers should be required to include these features in order to help maximize the potential participation and savings rates by their employees, and as a condition to certain favorable features and treatment of the Program. Participants would be permitted to opt out of the plan and the automatic escalation features the same as any 401(k) plan. The legislation that creates this concept should require the inclusion of the automatic enrollment and escalation features.

C. Contribution Limits – USERSPs should be subject to lower contribution limits than 401(k) and "SIMPLE" plans, but have higher limits than IRAs so that American workers have reasonable opportunities to save enough for retirement through these plans. The contribution limits should also be adjusted for inflation over time.

The Program includes adequate requirements and conditions to ensure that these plans are available to all employees of small employers and that all participants have the opportunity to save the maximum that they are willing and

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able to save. Other types of arrangements that have lower contribution limits will not allow most employees to save enough for retirement and are less attractive to the owners and decision makers who are responsible for making decisions to adopt retirement plans. This approach will encourage the formation of new plans by small employers while preserving and not detracting from existing 401(k) and SIMPLE plans.

D. Simplified Plan Documents – All USERSPs would use the same government approved prototype plan document. The use of a model plan by all service providers and employers would substantially reduce administrative costs and would relieve employers of the enormous and costly burden of ensuring that their plan documents comply with applicable legal requirements. The allowable plan features and plan limitations are summarized in Table1. In order to implement the Program, a plan document would have to be developed and approved for use.

Table 1

TYPE OF ENTITY	Any employer eligible to establish a 401(k) plan with less than 100 employees with at least one non-owner employee
EMPLOYER'S FISCAL YEAR	December 31st
PLAN YEAR	Calendar year
VALUATION DATE	Daily
TRUSTEE(S) OR INSURER(S)	Self-trusteed/employer or service provider
PLAN ADMINISTRATOR	Employer
CONTRIBUTION TYPES	Allowed: Elective Deferrals (Pre-tax only), Catch-Up Contributions, Limited Employer Matching Contributions, and Rollover Contributions Not allowed: Roth, After-tax and Profit Sharing Contributions
ELIGIBLE EMPLOYEES	No exclusions
CONDITIONS OF ELIGIBILITY	Conform to any Automatic-IRA rules
EFFECTIVE DATE OF PARTICIPATION (ENTRY DATE)	Conform to any Automatic-IRA rules
SERVICE CREDITING METHOD	N/A
VESTING	If employer match is allowed, no vesting would apply – would be 100% vested
VESTING FOR DEATH AND TOTAL AND PERMANENT DISABILITY	N/A
NORMAL RETIREMENT AGE	65
EARLY RETIREMENT DATE	None
COMPENSATION	Wages, tips and other compensation on Form W-2 for the plan year
SALARY REDUCTION ARRANGEMENT- ELECTIVE DEFERRALS	Up to the maximum amount allowed by law
Deferral Modifications	Can modify as of each payroll
Automatic Deferral Provisions	Required
Initial Automatic Deferral Amount	3%
Escalation of Deferral Amount	2% - up to a maximum of 11%
EMPLOYER MATCHING CONTRIBUTIONS	Voluntary, however, limited to 50% of the first 3% (or any formula that is determined to be the required initial percent for automatic-enrollment)
Allocation Conditions	None
EMPLOYER PROFIT SHARING CONTRIBUTIONS	None
FORFEITURES	N/A – No money subject to vesting
FORM OF DISTRIBUTIONS	Service providers' option
CONDITIONS FOR DISTRIBUTIONS UPON TERMINATION OF EMPLOYMENT	Distributions may be made as soon as administratively feasible following termination of employment
Participant Consent	For distributions over $1,000; provider option regarding distributions for the $1,000 to $5,000 range
HARDSHIP DISTRIBUTIONS	Allowed; the minimum amount of a distribution is $1,000; safe harbor conditions only; no requirement to suspend contributions for 6 months
IN-SERVICE DISTRIBUTIONS	Not allowed
LOANS TO PARTICIPANTS	Not allowed

E. Limited Plan Features to Prevent Savings Leakage – USERSPs would have limited plan features to prevent pre-retirement savings leakage.

USERSPs would not permit participant loans and would only permit hardship distributions that meet the safe harbor conditions that apply to regular 401(k) plans. Participants who take a hardship would not have contributions to the plan suspended. Pre-retirement distributions adversely affect workers' ability to reach their long term retirement savings goals and achieve financial security. The USERSP would limit these options so that participants are less likely to use their retirement savings for other reasons. These limitations are summarized in the table in Section D above.

F. Simplified Administration – USERSPs would not be subject to existing discrimination testing. The elimination of discrimination testing will substantially reduce the compliance administrative burdens. The requirements that all employers offer a plan and that such plans include mandatory enrollment offset the need for such testing by providing access to a plan for all employees and requiring employees to affirmatively opt out if they choose not to save. Moreover, data shows that significant numbers of employers who are unable to make meaningful contributions to their own plan due to discrimination testing failures terminate such plans.

USERSPs would not permit participant loans and would only permit hardship distributions that meet the safe harbor conditions that apply to regular 401(k) plans.

Nondiscrimination rules that apply to 401(k) plans are designed to ensure that pension benefits associated with plan deferrals and contributions do not disproportionately accrue to highly compensated employees. The rules are complex and not only increase administrative and compliance costs associated with offering a plan,[2] but in many situations make it very unattractive for small employers to establish plans. Removing the application of the nondiscrimination rules to employers eligible to use the USERSP would remove a major impediment to plan adoption, and prevent plan terminations when employers are otherwise unable to contribute to their own plans.

The SPARK Institute notes that exempting USERSPs from the discrimination testing rules will benefit lower paid workers overall without any potential harm. Although higher paid workers, who may be the decision makers or owners of the small employer, would not be subject to the contribution limits of these tests, that does not prevent other employees from contributing the maximum otherwise allowed under the plan.

[2] Every 401(k) plan other than "SIMPLE" plans, "Safe Harbor" plans or "Qualified Automatic Contribution Arrangements," must comply with a series of complex annual tests to prevent "discrimination" in favor of the group of employees referred to as "highly compensated employees." "SIMPLE", "Safe Harbor" and "Qualified Automatic Contribution Arrangements" each require a participating employer to contribute a specific percentage of compensation or an amount equal to a preset ratio of employee deferrals to the plan.

Moreover, the incentive of not having to comply with discrimination testing will likely expand access to plans and prevent terminations. Some opponents to this feature of the Program may believe that the discrimination testing rules provide an economic incentive to employers to increase contributions to low-paid workers for the purpose of enabling high-paid workers to receive a higher proportion of compensation in the form of benefits. While such arguments may have merit in the context of larger employers, they seem to provide little incentive for small employers at best, and perhaps hinder plan adoption at worst.

G. No Mandatory Employer Contributions – Employers would not be required to make contributions to the plan. However, limited voluntary employer contributions would be permitted.

As is the case for 401(k) plans generally, the USERSP would not mandate that employers contribute to the plan. However, the existing Tax Saver's Credit, which President Obama has recently recommended to be expanded, provides a government incentive for lower income workers to save for retirement through their employer-sponsored plan, even if the employer is not able to commit to, or afford to, provide the incentive.

Employers would be permitted to make limited voluntary contributions to the plan subject to the same limits that apply to 401(k) plans. As noted in Section II, D, voluntary matching contributions would be permitted for up to 50 percent of the first 3 percent of pay deferred by an employee, or any formula that is determined to be the required initial percent for automatic-enrollment plans. A voluntary matching contribution that meets these requirements would not be subject to the discrimination testing rules, as noted under Section F.

Despite efforts by policy makers over the years to establish plans, like the "SIMPLE," which were designed to lessen the compliance burden associated with plan sponsorship,[3] according to data from the Bureau of Labor Statistics' Employee Benefits Survey, only 30 percent of employers with a workforce of between 10-24 employees offer a workplace retirement plan and 45 percent of employers with a workforce between 25 and 99 employees offer a plan. Many studies and surveys of small employers (companies with up to 100 full-time workers) have sought to better understand the challenges presented by small employers which serve as impediments to the establishment of a retirement plan for their employees. While, as discussed elsewhere in this paper, administrative costs and burdens associated with establishing and running a plan play an important role, one study suggests that perhaps a more important explanation for the lack of plan sponsorship is the financial reality of running a small business.[4]

[3] SIMPLE plans were introduced in 1997 as a way to allow small employers to offer a retirement plan to their employees, without requiring compliance with a lot of complicated rules. For example, under a SIMPLE plan, each employee can defer a total of $11,500 in compensation, or $14,000 if they are fifty or older, but the employer must contribute a 3% match for employees who participate. There are no minimum participation rules and all employer contributions vest immediately.

[4] See The 2001 Small Employer Retirement Survey (SERS), sponsored by the non–partisan Employee Benefit Research Institute (EBRI), the American Savings Education Council (ASEC), and Mathew Greenwald & Associates (hereinafter, "SERS Study").

In this respect, the SERS study notes that for many small businesses revenue streams are uncertain and their employees tend to be lower paid with a preference for cash and non-retirement benefits. When viewed from this perspective, it is understandable why the imposition of a contribution obligation would serve as a strong disincentive to many small employers who might otherwise be inclined to establish a retirement plan for their employees.

H. **Simplified Investment Option Selection and Fiduciary Exposure** – USERSP investment options would be required to meet specified minimum requirements for broad based investment choices. Investment options can be chosen by either the employer, if it prefers to do so and the service provider's arrangement allows, or determined by the service provider as part of its product offering. Employers and service providers would be protected from potential liability for investment losses for investments that satisfy safe-harbor criteria specified under the Qualified Default Investment Alternative rules for auto-enrollees or as participant directed investments meeting the rules and conditions specified under ERISA Section 404(c).

Under the Program, a service provider could select and limit the investments that are offered as investment options to the plans and participants as part of its product structure, or permit the employer to select the investment options from a group of available options. Where the service provider "selects" the investment options as part of its product structure, the investment options would have to meet standards established by the DOL, including the use of a qualified default investment alternative ("QDIA") for new enrollees and all other situations where a participant does not give investment directions. Additionally, the provider's product would be required to include a broad range of additional investment choices that meet the conditions to qualify for protection under Section 404(c) of ERISA. Under this structure, the employer's fiduciary responsibility would be limited to prudently selecting and monitoring the service provider. The plan provider's activities would be deemed only as the offering of a product (which could include proprietary funds). A provider's "product offering" should not cause the provider to take on fiduciary responsibility for choosing the investment options used by plans that select the provider's product.

> ***A service provider could select and limit the investments that are offered as investment options to the plans and participants as part of its product structure, or permit the employer to select the investment options from a group of available options.***

Where the employer selects the investment options, instead of the service provider, the customary fiduciary requirements would apply to the employer. Employers acting accordingly should be able to rely on the QDIA, 404(c) and other safe harbors and exemptions that are available to employers under existing arrangements.

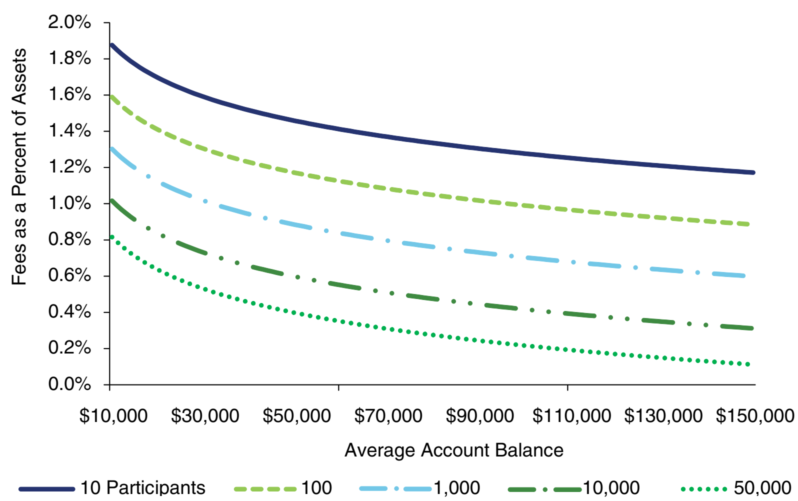
In order to facilitate this aspect of the Program, any enabling legislation should direct the DOL to issue guidance limiting the scope of an employer's fiduciary responsibilities to selecting and monitoring the service provider when the employer does not pick the investment options. The DOL should be further directed to issue guidance that clarifies the responsibilities of service providers that select the investment options as part of their product structures and extends the QDIA and 404(c) safe harbor to the extent necessary in order to limit service providers' potential fiduciary liability.

I. Multiple Employer Record Keeping Aggregation – In order to help reduce administrative costs and leverage potential investment option economies of scale among many participating small employers, record keepers should be permitted to aggregate assets across plans and employers, provided that individual plan and participant assets can be separately identified and accounted for.

In a recent study conducted by Deloitte Consulting, plan asset size was identified as the primary driver of fees. The study found that plans with fewer than 100 participants paid higher fees as a percentage of assets than larger plans (See Table 2).[5]

Table 2

Predicted Fees as a Percent of Assets by Average Account Size and Number of Participants (All Other Explanatory Variables = Means)



Source: Deloitte/ICI: Defined Contribution/401(k) Fee Study copyright 2009, Deloitte Development LLC.

[5] Defined Contribution / 401(k) Fee Study - Inside the Structure of Defined Contribution / 401(k) Plan Fees: A Study Assessing the Mechanics of What Drives the 'All-In' Fee, Conducted by Deloitte for the Investment Company Institute (Spring 2009).

Record keepers should be permitted to leverage the scale that can be created with large numbers of small plans by maintaining USERSP plans of unaffiliated small employers on their record keeping systems as a single plan. This would reduce the record keeping costs of implementing and maintaining large numbers of smaller plans. The assets of the plans would remain segregated and held in trust for each plan and participant and plan level reporting and benefit statements would be unaffected (i.e., each participant exchange would be maintained in account history).

Another possible advantage of this approach is that smaller plans that are record kept as a single plan may be able to use certain investment options or lower cost investment options that may not otherwise be available to each plan on an individual basis.

J. **Consolidated 5500 Reporting** – Service providers should be permitted to submit consolidated annual Form 5500 reporting at the service provider level for the plans it services.

The Form 5500 Annual Return/Report is the principal source of data available to the DOL, IRS and PBGC concerning the operations, funding and investments of employee benefit plans and forms an integral part of each agency's enforcement, research and policy formulation programs. It is a source of information for Congress and the private sector in assessing employee benefit, tax, and economic trends and policies. These uses must be balanced, particularly in light of the PPA guidance regarding small employers, between insuring adequate reporting and disclosure on the one hand, and the administrative costs and burdens attendant to maintaining a plan on the other hand.[6]

Service providers should be permitted to submit consolidated annual Form 5500 reporting at the service provider level for the plans it services.

Consolidated 5500 reporting would help reduce administrative costs for employers. In addition, particularly with the new electronic filing rules that require plan sponsors to obtain signing credentials and submit all reports, the ability to have a plan provider file a consolidated 5500 will reduce the amount of time and some of the fear associated with government reporting.

Consolidated reporting would also be appropriate for USERSP plans because the Program requirement, by definition, reduces the need for more complex informational reporting. These plans must use the same pre-approved prototype document, with limited availability for distributions and no loans. Additionally, these plans would not permit investments in products other than "eligible plan assets" as described in the instructions to Form 5500 SF.

[6] See 72 Fed. Reg. 64,731 – 64,732 (2007).

General Description of the Consolidated Reporting Approach – All USERSP plans would be eligible to report on the Form 5500 SF. That form includes information on general plan data (e.g., identification info, number of participants, etc.), financial data (e.g., income, fees, benefits paid, etc.), compliance information (e.g., late deposits, fidelity bond coverage, loans, black outs, etc.), and information concerning plan termination. No additional schedules or attachments are required.

The consolidated reporting approach will balance the need for individual plan information against the cost and complexity of requiring individual filings using the following general approach and guidelines:

1. The consolidated filing will include basic identification information on all plans included in the report. This will include information similar to what is currently requested in Part II, questions 1-5 of the current 5500 SF including the plan name, employer EIN, and number of participants at the beginning and end of the year. Each plan will be assigned a status code indicating whether it is the first year the plan is included in that service provider's filing, a year in which the plan transferred to a new service provider, a year in which the plan terminated, or a plan which was reported in the previous year and has not changed its status. This will enable the DOL to track plans and collect data in the same manner it does today with individual filings.

2. All plans will be required to sign off to the service provider on compliance questions similar to what is contained in Part V of the 5500 SF, but adapted to this product. In the event any question is answered in a way indicating a potential compliance issue, the plan(s) and associated issue(s) will be separately identified on a schedule attached to the consolidated report, or the plan will be required to file its own 5500.

3. Financial information similar to what is required in Part III, Questions 7 & 8 of the 5500 SF will be reported on an individual plan basis. This will include the plan's beginning and ending asset balance, contributions received and distributions paid, earnings from plan investments, and direct expenses paid from plan assets.

In order to facilitate this aspect of the Program, ERISA Section 104(a) and related regulations would be required. In addition, a new 5500 form would have to be created and the DOL would have to issue guidance with respect to the consolidated reporting.

K. Electronic Communications – In order to help drive better outcomes and reduce administrative costs, electronic delivery should be permitted to be the default delivery method for all participant communications. Participants would always have the option to request, via telephone, and receive hard copies of any and all information at no charge to them. Additionally, participants that do not have an email address would automatically receive hard copies. Participants would also have internet access to view, print and request the communications.[7]

Electronic delivery of communications will also allow for more personalized and timely communications. Electronic communications, via email and the internet, can be customized to each individual based on the participant's needs, interests and demographics. Studies show that workers are more likely to act on their investments if they receive information electronically.

In order to help drive better outcomes and reduce administrative costs, electronic delivery should be permitted to be the default delivery method for all participant communications.

Conclusion

The SPARK Institute believes that this Program can provide a cost-effective way for more employees to be able to save through workplace savings plans and to leverage the current 401(k) system infrastructure and experience. We note, however, that we oppose any mandatory employee savings program that requires the government to be the guarantor of a minimum rate of return, and that limits the investment options available to employees.

[7] According to a recent EBRI study, 91 percent of active 401(k) plan participants were under 60 at the end of 2007 and access to an Internet-enabled PC at home is generally above 80 percent among people under 60. Internet access by people age 55 and over has been growing at a fast pace (from 8 percent in 1997 to 64 percent in 2005). Additionally, 99 percent of all public libraries offer free public internet access.

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The SPARK Institute
714 Hopmeadow Street, Suite 3
Simsbury, Connecticut 06070
Ph: 860-658-5058
Fx: 860-658-5068
www.sparkinstitute.org

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