TOP STORY

Private Sector Defined Contribution Leaders Meet

NAGDCA held a special roundtable meeting for Industry members in April in Washington, D.C. The members gathered to hear from federal policy makers regarding legislative and regulatory developments that affect the defined contribution programs of state and local governments; as well as to discuss the legislative issues affecting the industry.

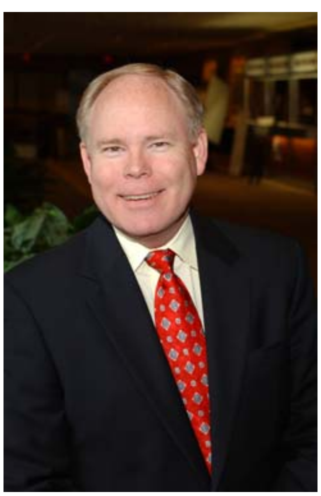
"Because of the important role the private sector plays in the defined contribution industry, it is important to bring legislative and operational leaders together to discuss and make recommendations on common issues," said Ralph Marsh, NAGDCA President.

Topics addressed included fee transparency, automatic enrollment, retiree healthcare, and SEC developments/mutual fund procedures as they relate to defined contribution plans.

NAGDCA Industry President, Brian McCleave, stated "The intent of the Roundtable was to provide a forum for Industry members to discuss debate and find common ground on administrative and legislative issues of importance. This is the third Roundtable for NAGDCA Industry members and it continues to prove itself as a valuable forum for the defined contribution community at large."

MARK YOUR CALENDAR:
2007 Annual Conference
September 15 - 19
Indian Wells, California
Hyatt Grand Champions Resort and Spa
Register online at: www.nagdca.org

PRESIDENT'S CORNER



As I prepare to write my final President's Corner message, I sit here and wonder which is the best direction to take. There is so much going on in the world today and in our own special retirement 'community', that it's very easy to drift from topic to topic. As always, legislation is a special area, but we at NAGDCA are very fortunate to have our very own expert, Susan White, to fill you in on those details. So I decided to let the expert give you that information, and I will report on the Association and where we are today.

This year was a very rewarding year for the Association. We have made several strides in achieving some of the goals we have set out to do. Major among them are:

We have continued our relationship with InFRE and IFEBP, as well as established new ones with The U.S. Financial Literacy and Education Commission. NAGDCA is currently working in a cooperative effort with the newly formed National Financial Literacy Network to develop a clearinghouse dedicated to financial literacy programs offered by state and local governments. This clearinghouse will be available to the general public and offer a multitude of resources that will assist in all spectrums of financial understanding.

To continue on with NAGDCA's stance on the importance of industry education, the Arthur N. Caple Foundation has been established. This year, through the wonderful support of NAGDCA and its members, 14 scholarships have been awarded to student across the country. These scholarships will assist students ranging from help with tuition to travel expenses to the annual conference. The foundation will not only allow for these scholarships to be awarded on an annual basis, but for continued research in retirement issues surrounding the defined contribution community.

NAGDCA has also continued its educational programming through webcasts, information brochures, and the planning of the annual conference. Yes, it's hard to believe that the 2007 Annual Conference in Indian Wells, California, is just around the corner. Information on the conference and sessions were distributed to members in May, and we anticipate this year's conference could lead to record attendance.

Also, we are working with several universities throughout the country to continue our highly successful Student Mentoring Program, which has led to many internships and job opportunities for past participants. I would also be remised not to mention the wonderful support that NAGDCA members have brought to this program by acting as mentors for these promising students.

In closing, I would like to thank the Executive Board and all the members for the opportunity to allowing me to serve you. As I wind down in what has been a very fast six years of service, I have seen many changes in the Association. In that span, I have seen federal legislation that has brought our plans up to speed with the private plans, the quarterly Newsletter has been given a face lift, and web casts have been provided to our members, allowing for frequent industry updates and educational opportunities. I believe NAGDCA now has tremendous exposure and recognition in the industry. These accomplishments came not from one person, but from a group of people committed to the Association and its *Vision*. Again, thank you for an exciting year, and I look forward to meeting you in Indian Wells.

INDUSTRY VIEWPOINT

Do you administer a public pension for employees not covered by Social Security? If so, you may be aware of two laws that can offset, or perhaps eliminate, Social Security benefits employees may have earned on the side or may be due from a spouse. Questions are understandable, given the complexity of these laws: the windfall elimination provision and the government pension offset. This article intends to clarify these government offsets.

Social Security Offsets: Policies Public Employees Love to Hate and Don't Understand

by Thomas Margenau, ©2007 International Foundation of Employee Benefit Plans

"I've heard through the grapevine that my Social Security will be cut in half because of our pension plan. What's the deal?"

"A co-worker just told me that I won't get a nickel of my wife's Social Security because of our pension. That isn't fair!"

"I understand an offset will prevent me from getting any Social Security. But surely I'll be covered by Medicare, right?"

The above questions and comments may be heard from those who work in the benefits or payroll department of a public agency not covered by Social Security. Conventional wisdom usually places the blame for these perceived Social Security benefit inequities on a law vaguely referred to as a government offset.

In fact, there are two provisions in Social Security law that may potentially impact employees due to receive a pension from a job not covered by Social Security. The first is the windfall elimination provision, which generally reduces a public employee's own Social Security retirement benefit. The second is the government pension offset, which impacts any Social Security spousal benefits employees might be due from a wife or husband's Social Security record. Employees may be affected by one or both of these laws.

Two Provisions

Most local and state government employees, as well as a growing share of federal employees, pay into Social Security just as everyone else does. In fact, approximately 70% of all state and local government jobs (including teachers in most states) are covered by Social Security. However, for those representing a portion of the 30% of public employees not covered by Social Security (including teachers in some states such as California and Texas), these laws will play a major role in pension and retirement planning.

If employees receive a pension from a job not covered by Social Security, but they have paid enough Social Security taxes in other jobs to qualify for a Social Security retirement benefit, that benefit will likely be reduced due to their government pension. The law requiring this reduction is the windfall elimination provision.

That same government pension will offset, and usually eliminate, any Social Security benefits employees may be due on a spouse's Social Security record. The law requiring this reduction is the government pension offset.

Why Are Most Jobs Covered by Social Security While Others Are Not?

When the Social Security Act was passed in the mid-1930s, most workers in commerce and industry did not have any type of retirement pension plan. Because they were expected to directly benefit from Social Security, they were covered by the new law. Over the next several decades, other large employee groups, such as farm workers and military personnel, were also covered under the Social Security umbrella. In the mid-1950s, the self-employed were added to the Social Security rosters.

Certain large employee groups, such as federal government employees and railroad workers, had already established pension plans before Social Security was added. Therefore, Congress decided to exclude them from Social Security. Also, at the time of Social Security's enactment, Congress felt it could not mandate a federal pension plan (Social Security) on state and local government entities, so employees of these agencies were given the choice of participating in Social Security. Of course, many of these entities established their own pension plans intended to operate independently of Social Security.

While many small and large government agencies did not accept Social Security coverage, over the years a high percentage of all state and local public employees opted to join the Social Security system. In 1983, sweeping changes altered the Social Security landscape following the recommendations of a presidential commission. All federal employees hired after December 31, 1983 were included in Social Security as were members of Congress, the president and vice president. State and local government employees were forbidden to terminate Social Security coverage after April 20, 1983. So today, railroad workers, a diminishing number of older federal government employees and about 30% of state and local public employees are the only large groups of workers in the United States not covered by Social Security.

That same presidential commission recognized that certain inequities in Social Security benefit payments were the direct result of these Social Security coverage issues. Public employees who worked for a relatively short time under Social Security received a windfall in Social Security retirement benefits that was intended only for long-term lower income workers. Many public employees were receiving spousal benefits from a husband's or wife's Social Security record although they did not meet the legal definition of dependency associated with those benefits. The result was, the commission recommended the passage of the two laws that became known as the windfall elimination provision and the government pension offset to deal with these inequities.

Windfall Elimination Provision
The windfall elimination provision reduces an employee's Social Security benefit, generally by about one-half. In other words, if the computerized estimate an employee impacted by this provision receives from the Social Security Administration indicates he or she is due $400 per month in a retirement pension upon reaching Social Security's full retirement age, that person can likely expect to receive about $200.

This is a very important point because if the Social Security Administration does not know if a potential retiree is impacted by the windfall elimination provision, it does not use the modified retirement benefit formula when sending annual benefit estimate statements. Therefore, retirement estimates in the Social Security statements sent to employees impacted by the windfall elimination provision are most likely wrong.

The key to understanding this provision is to realize that the word "social" in Social Security means something. Unlike private and other public sector pension plans, there are social goals built into the Social Security program. One of those goals is to raise the standard of living of lower income workers in retirement. This is accomplished through a benefit formula designed to give lower-paid workers a better deal than their more highly paid counterparts. Very low-paid workers could get a Social Security retirement benefit that represents up to 90% of their average lifetime earnings. This percentage is known as a replacement rate. In other words, Social Security benefits paid to the lowest-paid workers in our society are intended to replace 90% of their pre-retirement earnings. Those with average incomes (the middle class) generally get a 40% replacement rate. Those with higher incomes get a rate of approximately 30%.

The actual benefit formula the Social Security Administration uses to figure Social Security retirement benefits is updated annually and is further complicated by variables that are different for each year of birth. For example, a worker who turns 62 in 2007 would take the first $680 of average monthly earnings and multiply it by 90%; the next $3,420 by 32%; and the remainder by 15%. The Social Security Administration publishes a fact sheet, "Your Retirement Benefit—How It Is Figured," that explains the benefit computation formula. It is available on the Social Security Administration's Web site at www.socialsecurity.gov/pubs/10070.html.

In the author's opinion, the problem is that government employees and others who spend the bulk of their working lives not paying into Social Security are automatically treated as low-income workers by the Social Security Administration's computers. This is due to zeros on their Social Security earnings record for every year they spent in a non-Social Security job. Social Security's records don't show that they were actually working at another job and earning another pension. Instead, their Social Security earnings record simply shows gaps in their work history. So, when figuring their Social Security retirement benefit, the Social Security Administration's computers automatically use the formula intended to compensate a lower-income person. However, government employees can generally be classified as having average incomes, so they should get the same Social Security replacement rate paid to all middle-class workers. This is why a modified formula is used to refigure their benefits and give them the proper, and fair, replacement rate. For public employees impacted by this law, this modified formula replaces the 90% benchmark in the first step of the Social Security retirement formula with a smaller rate of usually 40%. The desired effect is to eliminate the windfall paid to middle-class public employees usually intended for lower-class workers (thus the name windfall elimination provision). Or, in other words, the windfall elimination provision takes a public employee from the 90% (low-class) replacement rate to a 40% (middle-class) replacement rate.

What Does That Mean in Real Money?

If an employee is affected by the windfall elimination provision, there is a simple formula that can be used to refigure his or her benefit. For example, if the retirement estimate in his or her Social Security statement is $612 or more, subtract $340 (or half of the public pension, whichever is less). If the retirement estimate in his or her Social Security statement is $611 or less, multiply the estimate by four and divide by nine.

The Social Security Administration has an online calculator for those impacted by the windfall elimination provision. It can be found at www.socialsecurity.gov/retire2/ anyPiaWepjs04.htm.

An Exception to the Windfall Elimination Provision

The modified windfall elimination provision formula shown above applies only to people who have 20 or fewer years of substantial Social Security earnings. The table on page 37 gives a year-by-year breakdown of what the government considers substantial earnings:

If an employee has 30 or more years of substantial Social Security earnings, the windfall provision won't apply and the employee's Social Security benefit will not be reduced. If an employee has between 20 and 29 years of substantial earnings, his or her Social Security benefit will be only partially reduced. Instead of being cut roughly in half, it will be reduced by about 5% to 45%, depending on the number of years of substantial earnings on the person's record. The more years of earnings, the less the reduction will be. The online windfall elimination provision calculator on the Social Security Administration's Web site will figure the reduction that applies.

There are other exceptions that apply, such as for railroad workers, some employees of nonprofit organizations and those who worked in non-Social Security jobs prior to 1957. For a complete list of exceptions, see www.socialsecurity.gov/pubs/10070.html.

Why Some Employees May Want a Second Job

Some employees may not be eligible for a Social Security retirement benefit (windfall elimination provision or not) if they do not have the 40 credits necessary to qualify for such benefits. However, employees who have close to 40 credits should consider taking a part-time job just to get over the threshold. With 39 or fewer credits, an employee won't collect a nickel from Social Security. With 40 or more credits, he or she will collect a benefit that will be subject to the windfall elimination provision and may be reduced to an amount less than $100 per month. And $100 in nickels is better than no nickels at all.

An employee can take a part-time job earning as little as $4,000 per year and receive four credits from Social Security. (That's the maximum payable in any one year.) Public employees significantly under the 40-credit threshold will have to decide if it is worth the effort to work at a Social Security-covered job for up to ten years to qualify for a very small monthly payoff from the system.

Government Pension Offset

The windfall elimination provision impacts an employee's Social Security retirement benefit. The government pension offset impacts Social Security spousal benefits and affects employees who will collect a pension from a job not covered by Social Security.

The government pension offset essentially states that a public pension paid to employees not covered by Social Security will offset (and generally eliminate) any benefits they may be due on a spouse's Social Security record.

The Simple Government Pension Offset Formula

Unlike the complicated windfall elimination provision discussed above, the government pension offset formula is simple; the Social Security Administration must deduct an amount equal to two-thirds of an employee's government pension from any wife's, husband's, widow's or widower's benefits he or she might be due from Social Security. Because public pensions are often substantially higher than spousal benefits paid under Social Security, this rule generally means that an employee impacted by the government pension offset will not qualify for any benefits on a spouse's Social Security record.

Why the Offset?

Benefits that Social Security pays to wives, husbands, widows and widowers are dependent's benefits. These benefits were established in the 1930s to compensate spouses who stayed home to raise a family and were financially dependent on the working spouse. However, as more and more couples became employed, they each earned their own Social Security retirement benefits. Social Security law has always required Social Security Administration to offset one retirement benefit against another. For example, if a woman worked and earned her own $800 monthly Social Security retirement benefit but she was also due a $500 wife's benefit on her husband's Social Security record, the Social Security Administration could not pay that wife's benefit because her own Social Security benefit offsets it. However, if that same woman was a government employee who did not pay into Social Security and earned an $800 public pension, there was no offset (prior to the government pension offset law) and the Social Security Administration was required to pay her a full wife's benefit in addition to her government pension.
The government pension offset rule exists to ensure that employees who collect public pensions are treated the same way as those who collect Social Security retirement pensions.

Exceptions

There are a few exceptions to the government pension offset. They apply primarily to state and local government employees whose public pension was based on a job where they were paying Social Security taxes during the last five years of their employment, or to "civil service offset" employees. (A civil service offset employee is a federal employee with at least five years of prior civil service experience, rehired in 1984 or later following a break of more than one year in government service.) For a complete list of exceptions to the government pension offset rules, see the Social Security Administration's Web site, www.socialsecurity.gov/pubs/10007.html.

An Example That Explainsthe Fairness of the Government Pension Offset

Many public employees impacted by government pension offset think the law is unfair. They believe they are being cheated out of Social Security benefits that everyone else receives. For example, Bob and Carol—and their neighbors, Ted and Alice—live in a nice suburb of San Diego. Both Bob and Carol worked all of their lives at jobs covered by Social Security. In other words, Social Security taxes were deducted from both of their paychecks.

Ted also worked at a job covered by Social Security, however, his wife, Alice, was a teacher in San Diego. California teachers pay into the state teachers retirement system, but they do not pay into Social Security.

Bob retired and is receiving $1,200 per month in Social Security retirement benefits. For most of her life, Carol actually made more money than Bob, so she is receiving a Social Security retirement pension of approximately $1,500 per month. Carol cannot receive (and frankly, doesn't expect) any wife's benefits on Bob's record because her own Social Security benefit precludes any spousal payments. In other words, Carol's own retirement benefit offsets any wife's benefits she may have been due on her husband's record. In addition, Bob cannot receive a husband's benefit on Carol's record because his own retirement benefit would offset it.

Ted is receiving roughly the same Social Security benefit as Bob, about $1,200 per month. Alice is receiving a $3,000 monthly California teacher's pension. Before the government pension offset was in place, Alice would have received a $600 dependent wife's benefit from Social Security in addition to her comfortable teacher's pension. But again, the government pension offset prevents this from happening. Yet Alice, reflecting the views of many public employees, is upset because she cannot receive a wife's benefit on Ted's Social Security record. Alice believes she and other government employees are being singled out for Social Security penalties. What she doesn't understand is that the law treats her the same way her neighbor Carol is being treated. Again, it says that neither woman will get a dependent wife's benefit from Social Security because each is receiving her own retirement pension.

An Important Medicare Message
Although employees may not qualify for monthly cash benefits on a spouse's Social Security record (because of the government pension offset), they can still receive Medicare on that spouse's record, assuming they are aged 65 or older and cannot receive Medicare on their own records.

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For information on ordering reprints of this article, call (888) 334-3327, option 4.

Thomas Margenau of Fort Collins, Colorado recently retired from the Social Security Administration. During his 32 years of service, he was director of the Social Security Administration's public information office, deputy press officer and speechwriter to the Commissioner of Social Security. Margenau writes a nationally syndicated newspaper column on Social Security issues. Margenau received an M.A. degree from the University of Wisconsin.

Automatic Enrollment and Qualified Default Investment Alternatives: Are They Right For Your Plan? Our Analysis Indicates They May Be Best For Both Plan Sponsors and Participants *…And Eligible Employees*

By Great-West Retirement Services

At the request of many of our plan sponsors, this issue of *Focus on 457* addresses three questions:

- **Is Automatic Enrollment a good idea?**
- **Which Qualified Default Investment Alternative (QDIA) has the greatest chance of helping participants in the long run?**
- **Should you change your default investment option even if you do not offer Automatic Enrollment?**

The Pension Protection Act of 2006 (PPA) provided guidelines for automatic enrollment and automatic deferral increase features for ERISA plans. While governmental plans are not subject to ERISA, you may wish to adopt the PPA standards as a best-practice guide for plan governance. The provisions for Automatic Enrollment and Qualified Default Investment Alternatives (QDIA's) in the PPA have prompted many governmental plan sponsors to take a closer look at all three of the questions above.

Executive Summary of Our Findings

Question #1: Is Automatic Enrollment a good idea?

Our Conclusion: Automatic Enrollment is arguably the single most important action you can take as a plan sponsor.

Most plan sponsors spend a considerable amount of time evaluating the plan investment options made available to participants and the individual performance of each of the funds. Studies have indicated, however, that individual fund performance is one of the least important variables in determining retirement wealth for plan participants.[1]

One of the more recent studies on this topic concluded that the five most important factors in accumulating retirement wealth rank as follows in terms of their impact on retirement wealth accumulation:[2]

1. **Deferral rates**
2. **Diversification/asset allocation**
3. **Rebalancing behavior**
4. **Age-appropriate changes**
5. **Individual fund performance**

Although individual fund performance is important, the Putnam study, as well as a number of others, concluded that the other four factors have a more significant long term impact on retirement savings accumulation. With deferral (saving) rates ranked as number one, it stands to reason that getting employees enrolled in the plan is essential. Automatic enrollment with automatic deferral increases accomplishes two things:

- Participants enter the plan at the earliest possible date; and
- A savings (deferral) rate is set at a reasonable level and increases over time unless the participant elects an alternate amount.

Since plan participation and deferral rates are the most important factors in determining long term retirement savings, automatic enrollment with automatic deferral increases is the single most important step you can take to help employees save for retirement. While the other four elements listed above are important, they are not as important as deferral rates over the long term. [3]

Question #2: Which Qualified Default Investment Alternative (QDIA) has the greatest chance of helping participants in the long run?

Our Conclusion: Managed Accounts.

The proposed Department of Labor (DOL) regulations identify three Qualified Default Investment Alternatives (QDIA's) for plans with an Automatic Enrollment program:

- **Target Retirement Date Funds; or**
- **Balanced Funds; or**
- **Managed Accounts**

Our findings (as summarized in the table below) indicate that managed accounts provide the best long term opportunity for the participant for three primary reasons:

- Portfolio selection is more personalized since the participants' age, retirement objectives, other household assets, spouse/partner income and a variety of other factors are taken into account. This is not the case with a balanced fund or a target-date fund.

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[1] "DC Plans Missing the Forest for the Trees" by Putnam Investments Strategic Research, February 16, 2007.
[2] "DC Plans Missing the Forest for the Trees" by Putnam Investments Strategic Research, February 16, 2007.
[3] "DC Plans Missing the Forest for the Trees" by Putnam Investments Strategic Research, February 16, 2007.

- Our experience indicates a high degree of misuse of target-date funds. In some situations, the misuse is so high as to be completely counterproductive.

- Although the PPA provides a level of fiduciary protection to ERISA plan sponsors who adopt any QDIA option for their plan, the managed account provider is also a fiduciary with respect to the investment of participant accounts. This additional protection is not available under the other two options.

The table on the following page summarizes the key elements of each QDIA and explains why managed accounts are likely the superior choice.   We invite you to read the full analysis of this important topic in the background section of this document.

Qualified Default Investment Arrangements (QDIA)
Comparison of Balanced funds, Target-Date Funds and Managed Accounts

	Balanced Funds	**Target-Date Funds**	**Managed Accounts**
Static or Dynamic Election	Static	Static	Dynamic
Reflects Age Changes	No	Maybe	Yes
Reflects Other Life Changes	No	No	Yes
Considers Participant Assets Outside the Plan	No	No	Yes
Considers Spouse/Partner Assets Outside the Plan	No	No	Yes
Considers All Assets in the Plan to Determine Portfolio for Participant	No	No	Yes
Considers Personal Retirement Age	No	Maybe	Yes
Considers Life Expectancy	No	No	Yes
Plan Participant Fiduciary Protection	No	No	Yes

Question #3: Should you change your default investment option even if you do not offer Automatic Enrollment?

Our Conclusion: If your default investment option is a fixed fund or a money market fund, it is time for you to take a serious look at the alternatives.

Every plan sponsor knows that it is not a good idea for participants to invest all of their retirement savings in a fixed-income fund for their entire working career. Yet, when participants are defaulted into a fixed-income or money market fund, the vast majority of participants do not reallocate those amounts for a very long period of time, if ever. Studies show that most participants never make regular changes to their investment options or rebalance their funds.[4] A large number never make any change at all. Inertia takes over and many participants are stuck in a fund that is too conservative.

It is time to make inertia work *for* plan participants and not *against them* by changing your plan's default option to an asset allocation fund, target-date fund, or better yet, managed accounts. Even if you are not considering adding Automatic Enrollment to your plan, reconsidering your current default investment option may be wise.

We invite you to read the following in-depth discussion of how we arrived at our conclusions.

Automatic Enrollment Programs Are Easy to Implement In Some States But Not In Others

As described in the August 22, 2006 edition of *Focus on 457*, (http://www.fascore.com/PDF/gwrs/Aug2006_22_457.pdf) the PPA provides guidelines for plan sponsors wishing to offer automatic enrollment with automatic deferral increases to their employees. A number of governmental plan sponsors are already planning to add such a feature. In some states, governmental plan sponsors may offer automatic enrollment without employee consent. Some state laws, however, prohibit employers from deducting any amount from an employee's paycheck unless employee consent is obtained. As of the date of publication of this issue of *Focus on 457*, the situation in each state may be summarized as follows:

May Offer Automatic Enrollment[5]		Current Law An Impediment To Automatic Enrollment	
Nevada	Ohio	California	New Jersey
Montana	Maine	Oregon	Rhode Island
South Dakota	Utah	Washington	Connecticut
Kansas	Colorado	Idaho	Vermont
Missouri	Texas	Wyoming	New Hampshire
Louisiana	North Carolina	Alaska	New York
Mississippi	Virginia (recent change)	Arizona	Michigan
Wisconsin	Indiana (recent change)	North Dakota	Illinois
Alabama		New Mexico	Hawaii
Georgia		Minnesota	Kentucky
Florida		South Carolina	Iowa
West Virginia		Tennessee	Oklahoma
		Maryland	Pennsylvania
		Delaware	

Minimum wage laws are an issue in Arkansas, Massachusetts and the District of Columbia.

Legislation has already been signed into law in Indiana and Virginia amending state and local governmental payroll statutes or anti-garnishment laws. Indiana's automatic enrollment program is effective July 1, 2007 and the Virginia program is effective January 1, 2008. Similar legislation has been proposed or is being reviewed in some other states. Alaska has an exemption for the automatic enrollment feature of its new mandatory defined contribution plan implemented in 2006.

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[4] 98.4% of participants don't make regular allocation changes, and 60.4% do not do a fund transfer according to a Great-West Retirement Services study of participants' accounts over a 20-year period (1985-2004).

[5] Governmental Plans ok. Some issues may exist for non-governmental, non-ERISA plans in certain states.

Many employers in the states where the current law requires employee signature before amounts may be withheld from their paychecks are asking employees to sign a consent form on the first day of work as part of their orientation package. This allows the employer to implement an automatic enrollment program while the state laws are being reviewed and revised.

Qualified Default Investment Alternative (QDIA)

Employers wishing to take advantage of the fiduciary protections provided by the PPA must select a "Qualified Default Investment Alternative" (QDIA) for the investment of contributions for participants who do not specify an investment option.

Nearly all defined contribution plans have a "default investment option," normally a fixed account, a money market fund, or another conservative investment option designed to preserve principal. *Under the proposed DOL regulations, however, a QDIA may not be a fixed account or money market fund, but rather must be:*

- **Target Retirement Date Funds; or**
- **Balanced Funds; or**
- **Managed Accounts**

The exclusion of fixed accounts and money market funds sends a clear signal that participants should be encouraged to be in a well-diversified, professionally managed investment arrangement. At the time of this writing, the DOL has yet to finalize the QDIA regulations, due mainly to the unusually large number of comments received from concerned taxpayers. It is not surprising that a number of the comments are from fixed-income investment providers who want fixed-income options included as a QDIA. The comments on QDIAs in this edition of *Focus on 457* are relative to the requirements as we currently understand them[6], although they may be modified by the DOL when the final regulations are issued.

If a governmental plan sponsor offers automatic enrollment, one of the three QDIA options should be considered as the default investment option. In fact, using a QDIA is a best practice for governmental plans without an automatic enrollment feature.

Which QDIA is Best For Your Plan?

The most appropriate QDIA for your plan will depend on a number of factors, including your overall strategy for providing participants with professional investment management alternatives. The following discussion of the three types of QDIAs explains how they compare to one another.

Balanced Funds

Of the three QDIA options available, the balanced fund option is generally viewed as the least "personalized" when compared to the other two (target-date funds or managed accounts). A balanced fund may not be the best default option, however, because it is a "one size fits all" solution that may be inappropriate for participants as their *only* long-term asset management solution.

A balanced fund is a relatively static mix of stocks and bonds, or stock and bond funds in the case of a balanced "fund of funds". In nearly every instance, a balanced fund is too conservatively managed for younger participants while being too aggressive for participants nearing retirement. Because the fund is managed the same way for a 25 year old participant as it is for a 60 year old participant, the best that can be said is that overall, the fund is inappropriate for the average participant. While balanced fund managers argue that a diversified, pooled fund is the same concept as managing a large pool of assets supporting a defined benefit plan, the

[6] Published in the Federal Register September 27, 2006

comparison is flawed in two key areas. First, in a defined benefit plan the plan sponsor bears the investment risk so the participant is not affected by the actual performance of the fund. This is not the case in a defined contribution plan where the participant bears the investment risk. Secondly, the balanced fund manager must ultimately wrestle with accurately defining the primary investment objective of the fund during the investment phase: whether assets are to be invested primarily for younger participants with a greater tolerance for risk, or primarily for the benefit of older participants nearing retirement. It would be impossible to develop an investment policy for a single "balanced" fund that serves both constituents. In theory, the balanced fund manager must determine the risk level and portfolio composition that he or she deems consistent with the profile of the plan as a whole. Managing one fund that is intended to serve all participants equally regardless of age, risk tolerance or individual circumstance would be a difficult task.

One of the arguments in favor of balanced funds is that they are less expensive to operate than asset allocation funds or managed accounts. This may or may not be accurate, but in any event, any comparison of fees alone would be very misleading. You should compare historical yields of the various alternatives, along with the fees charged to operate them.

Finally, some proponents of balanced funds as the QDIA indicate that it is the simplest alternative and thus a good choice for plan sponsors preferring limited involvement in the QDIA selection and management process. This would be particularly true if a pre-packaged balanced fund was selected. They argue that participants who want to diversify investments will make their own selections. The primary problem with that logic is that the majority of participants never move their money out of the default investment option. If that is the case, you need to carefully consider whether a balanced fund is the most appropriate default investment option for participant funds knowing that the money may remain in that fund for decades, and that balanced funds do not take the individual's circumstances into account.

Target Date (or Lifecycle) Funds

Aside from their use as a QDIA, target date (or "lifecycle") funds are being heavily promoted by firms that offer such funds, and by some consulting and investment management firms. Some proponents have declared them the latest "must have" type of fund for defined contribution retirement plans. In case you are not familiar with the concept, here is how they work:

- A series of funds are created that have "target" retirement dates. In general, the target dates have five year intervals. For example, one fund is for participants planning to retire between 2010 and 2015, while another is for participants planning to retire between 2015 and 2020, and so on. That means the usual number of target-date funds offered by most vendors is 10. Some managers offer funds in 10 year increments, resulting in five funds, with a possible sixth for providing income during retirement.

- These funds are usually "funds of funds", which means they invest in other mutual funds. The underlying concept is that participants should invest more conservatively as they grow older. Thus, the mix of allocations to the underlying funds changes over time to become more conservative as the fund nears the range of target dates. The rate at which the mix of underlying allocations to equity and fixed income options changes is often referred to as the "glide path".

Target-Date Funds Are Not New

Target-date funds are not new. Mutual fund companies have been offering them for years, and some have a history of 10 years or more. The concept is very similar to "risk-based funds" which are tailored to the degree of risk selected by the participant. For example, a collection of risk-based funds generally consists of five: conservative, moderately conservative, moderate, moderately aggressive, and aggressive. In some cases, the plan sponsor has simply opted for three risk-based funds (aggressive, moderate, and conservative).

The main difference between risk-based funds and lifecycle funds is that the investment allocation of the risk-based funds remains *static over time*. If a participant decides their risk tolerance has changed, they must select a different risk-based fund. For target-date funds, the allocation *changes over time,* as participants in the fund age.

An Old Concept That May No Longer Be Relevant For Many Participants

The underlying premise (that a participant should invest more conservatively as they age) is the very foundation of target-date funds. It is an old concept and one that (in theory) is sound if you want to reduce your risk of loss as you get closer to needing your money. The problem is, for our contemporary society and, in particular government employees, it is a concept that may not only be outdated, but actually counterproductive.

A “one size fits all” fund for everyone who is the same age (or within the same age range) can never take into account personal lifestyle differences, post-retirement or second-career plans, survivorship needs, or even something as simple as the retirement income of their spouse or partner, or their difference in age. Collective management of a group of people with similar ages might have worked well in the 50’s and 60’s when the work force was more homogeneous and “retirement” was more traditionally defined.

Today, the period following employment may not even be a traditional “retirement”. Many workers have plans for a second career or have income from other sources (such as a pension from a governmental employer). In many instances, these employees do not need their defined contribution funds immediately when they stop working. Or, if they do, perhaps they use some of these funds for lifestyle adjustments and keep the remaining funds invested. With greater longevity, many “retirees” may expect to live for as long as 20 or 30 years. Even the word “retirement” is no longer a relevant term for many who stop working in one career and then move to another during a later stage of life.

We also know, from our own research and that conducted by others, that not everyone of the same age has the same risk tolerance or investment objectives. To the contrary, we found that employees of the same age grouping could have dramatically different investment, lifestyle, and risk tolerance objectives[7]. Some studies have strongly challenged the age-risk correlation and categorized individuals by generation.[8] Other studies found a closer correlation in classifications such as single, young families, baby boomers and pre-retirees.[9] Therefore, the correlation between age and other lifestyle elements is just simply not precise, and in many cases, quite inaccurate. When you consider that the age-risk issue is the basic premise of target-date funds, it is unsettling, at best, because the correlation upon which it is based is largely inaccurate in the contemporary workforce. It is a premise that simply isn’t true for most people.

Target-Date Funds May Be Even More Inappropriate for Government Employees

If you are a governmental plan sponsor considering target-date funds, the first fact you have to deal with is that virtually all the “pre-packaged” target-date funds from the mutual fund industry were created for the corporate sector. In particular, they were designed for the individual investor

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[7] Focus group research on investment advice and fund management for government employees, conducted by Great-West and Advised Assets Group, LLC in 2004. Details of this research are available to Great-West clients on request.
[8] Center for Retirement Research, “Retirement at Risk: A New National Retirement Risk Index”, June 2006
[9] MetLife Fifth Annual National Survey, “Study of Employee Benefits Trends”.

and the corporate 401(k) market. Why is that something you should be concerned about? There are several reasons:

- The overwhelming majority of governmental employees are covered by a defined benefit plan, whereas the majority of the corporate workforce is not. Therefore, these funds are often managed to serve participants who will rely upon them as their sole (or major) source of retirement income. For many governmental employees, this is simply not the case.

- The range of retirement dates for governmental employees is quite large, especially considering the fact that public safety personnel can retire much earlier than their public and private sector co-workers.

- If a "one size fits all" fund for everyone the same age doesn't fit the corporate workforce (for lifestyle reasons we pointed out previously), then it is even less relevant to government employees.

Pre-Packaged Funds: Guess What You'll Find?

You see them advertised all the time on national television, in magazines and newspapers. They have catchy names, and are made attractive in glossy advertising campaigns that cost millions. These pre-packaged or "off the shelf" target-date funds, some of which have ten years of history or more, are heavily promoted. While these funds are easy to implement there are some important considerations worth noting before a plan sponsor deems them appropriate for their plan:

- Not surprisingly, with a few exceptions, the majority of these pre-packaged funds consist primarily or entirely of the managers own proprietary funds.

- When we examined one major fund company's "pre-packaged" target-date fund offerings, we found that most, if not all, of them consisted exclusively of their own funds. For example, all 23 holdings of their 2040 fund and all 25 holdings in the 2010 fund were the manager's proprietary funds. A second major fund company was similar with all 10 funds in their 2040 fund and all 14 holdings in their 2010 fund being proprietary funds. There was not a single outside fund in the portfolios.

This should be a concern to you unless you have chosen to use a bundled, proprietary plan design platform with recordkeeping and funds from one vendor. The majority of governmental plan sponsors, particularly larger plans, however, prefer the unbundled, open-architecture platform allowing them to select investment offerings on a *"best of class"* basis, with no preference for any particular fund manager. Every fund is selected on its own merits, based upon the plan's investment criteria. Selecting a pre-packaged series of target-date funds undermines the open architecture approach to fund selection.

Here's why this can be problematic:

- Employees are often confused when the investment options for the core funds differ from the underlying funds in the target-date funds. If you fulfilled your fiduciary responsibility by carefully selecting the core funds, why aren't they offered in the target-date funds?

- The time and effort you spent selecting and monitoring your fund offerings will be undermined if you elect to use pre-packaged funds over which you have no control. Even worse, you won't be applying the investment guidelines used to choose the core funds.

- Plan sponsors who select funds on a "best of class" basis know that no single investment manager or mutual fund company offers all the best performers in every asset class. Your employees may be expecting you to apply the same independent and objective criteria to the target-date funds that you use in selecting the core investment options.

- Last year a large governmental plan sponsor discovered that the target-date fund vendor they chose in a public bidding process changed the asset allocation of each fund and to structure each portfolio more aggressively. Although the plan sponsor objected to the changes, the mutual fund company went forward with the changes.

- All fees should be adequately disclosed to participants. Most funds have expenses on the underlying funds in the portfolio, plus an additional fee to manage the fund itself (a "fund of funds").

- There are some differences in fiduciary protection, as outlined in the next section.

Finally, if you elect to use target-date (lifecycle) funds be sure you understand how the funds are constructed, and what the fund management policies are. One recent article published by JP Morgan Asset Management said that standard fund industry assumptions are oversimplified in managing target-date funds and in fact are fatally flawed when compared to actual participant behavior.[10] The JP Morgan report says that the underlying assumptions in many target-date funds do not reflect actual spending and saving behavior of the participants in the funds, particularly since the report says that participants contribute less, borrow more, and have less in salary increases than assumed by the managers of the funds. It claims that the funds are missing the mark in providing retirement security to those who need it most. The point is that not all target-date funds are managed the same, and before a plan sponsor selects these funds as their QDIA, they have to know much more about them.

Fiduciary Liability Implications

If a plan sponsor selects a vendor to provide managed account services to their participants, that vendor is a fiduciary with respect to the managed account advice service. The vendor assumes fiduciary responsibility for the managed account or investment advice service for all participants who elect that service. The only fiduciary protection offered plan sponsors who choose to use pre-packaged target-date funds is through the QDIA regulations. The fiduciary liability issue is but one factor that should be evaluated when selecting target-date funds in addition to or in lieu of managed accounts or investment advice services.

What About Custom Target-Date (Lifecycle) Funds?

Larger plan sponsors can elect to establish their own custom target-date asset allocation funds rather than buying pre-packaged funds. If your plan is large enough to economically and administratively offer custom funds, they do have some advantages:

- The target-date asset allocation funds may consist solely of the underlying core funds in your plan, which often makes more sense to plan participants.

- Alternatively, one or more non-core funds with characteristics which make it inappropriate to offer on a "stand alone" basis may make sense when offered in a "fund of fund" environment.

- The individual or entity that designs the asset allocation for each fund and hires and fires the underlying fund managers has fiduciary responsibility with respect to the fund's

[10] "Ready! Fire! Aim? How some target date fund designs are missing the mark on providing retirement security to those who need it most", by JP Morgan Asset Management, March 2007

performance. Many plan sponsors therefore choose to hire an investment consultant to establish and monitor their custom target-date funds. This can be expensive. It is important to decide whether all the participants in the plan will bear the cost of this service, or only those who use the target-date funds. In the latter case, the costs of fund management, compliance and recordkeeping can be included in the overall pricing for the fund (determination of the share price or net asset value), which is generally more equitable. Charging all participants for the costs of the custom fund management raises a number of issues, including disclosure of that fact to all participants, including those who do not use the funds.

- A plan sponsor establishing and operating their own custom target-date funds must carefully consider the legal, regulatory, and disclosure requirements. Upon request, Great-West will send you a complimentary Briefing Document titled: "Asset Allocation Profiles as Investment Options –February 2007". This document discusses the administrative, regulatory, and disclosure requirements for custom asset allocation funds in more detail. Among many other issues, it is important to structure the funds and make disclosures properly so as to avoid registration under the Investment Company Act of 1940.

Carefully Consider the Motivation From Potential Vendors, and Who Has Liability for What Services

As discussed at the opening of this article, target-date funds are the current hot topic in the defined contribution market. Some professionals think they are a key ingredient for a successful plan, while others think they are a passing fad that is fraught with problems, or may actually be counterproductive.

The desirability of such funds to a mutual fund or investment manager who receives fees for managing them is obvious. The fees paid to lawyers and investment managers or consultants for custom target-date funds may not be so obvious. Many investment managers and consultants can provide asset allocation and rebalancing-management services for custom target-date funds. If you are going to pay a fund manager to manage your custom target-date funds, you need to carefully consider how many participants will benefit from this service and how it will be paid for.

One reason more and more plan sponsors are opting for managed account services is because only those participants who use the service pay the fees. While some plan sponsors have made it mandatory to participate in managed account services, virtually all of them offer an "opt-out" feature. This makes the overall fee structure for a managed account program more equitable than spreading the costs of the target-date funds among participants who have not elected to use these funds.

Finally, make sure that you, as the plan sponsor and your target-date fund manager understand your respective responsibilities. The target-date fund manager is responsible for, among other things, determining the asset allocation in each target-date fund as well as determining when and how often to rebalance the portfolio. In addition, the target-date manager is responsible for determining when and how each portfolio should be adjusted as the participants in that fund begin to age and become closer to the target-date of the fund. Sometimes this process is called the "glide path" to adjust each portfolio over time. In addition to hiring and evaluating the fund manager for any custom target-date funds, the plan sponsor should also determine key policy questions such as:

- Fiduciary liability in the event one or more participants are unhappy with the results of the target-date fund, or the "glide path" used by the manager. Does your fund manager have (or accept) fiduciary liability and if so, how much and what financial resources do they have?

- What is your policy if you discover that one or more funds have a sizable percentage of participants in that fund that are not within the target age range of the fund? What action do you take, if any, to let participants know they may not be in the "right" fund for their current age? Does the fund manager make any adjustments in that regard?

- The plan sponsor needs to be certain that the way the funds are managed and presented to participants does not make them subject to the registration as an investment company under the Investment Company Act of 1940 (see the Briefing Document on Asset Allocation Profiles dated February, 2007 available to Great-West Retirement Services plan sponsors).

Target-Date Fund Management: Conflict of Interest or an Economic Convenience?

Many consultants or potential target-date fund managers are quite objective in pointing out the above risks and benefits. Some firms will offer to provide overall investment consulting services ***or*** target-date fund management services, but not both. Others will agree to, or prefer to, do both. It is up to you to determine which is most appropriate for your plan when custom funds of any type are involved.

Some plan sponsors have taken the position that a plan consultant who recommends the use of custom target-date funds (or any particular investment option) can not then be used to manage such funds because of a potential conflict of interest. The issue may become more complicated if you use the same consulting firm to evaluate all core investment options as you use to manage the asset allocation funds. Some plan sponsors have not deemed it appropriate for the same consultant who evaluates the core funds to also evaluate their own performance on the target-date funds. Their position stems from the question whether you would let one of your investment managers evaluate their own performance on a fund they manage. If you take this position as well, then it will likely mean you may need two investment consultants if you offer custom target-date funds – one to evaluate all core options and one to manage the custom target-date funds. On the other hand, some plan sponsors have taken the position that having one consultant evaluate all the funds, and manage the asset allocation funds at the same time are a matter of economic convenience and do not pose a serious conflict of interest. When in doubt, seek the advice of counsel in this regard since it is easier to evaluate your liability before any such conflict arises in a lawsuit or fiduciary action from another party.

Despite the issues above, larger plan sponsors will likely prefer to create and manage their own target-date funds, if you choose to offer them at all. Assuming you actively monitor and groom your core funds, you may be able to offer target-date that have lower operating expenses and greater fund diversification than pre-packaged retail funds. Plus, you can be certain that all of the funds in your plan, including the target-date funds, are subject to the same evaluation and screening process. The larger the plan, the easier and more economical it is to offer custom funds of any type.

And Finally, A Very Important Point: How Participants Use These Funds

Plan sponsors who decide to offer pre-packaged target-date (lifestyle) funds, or create custom funds of your own need to have realistic expectations regarding usage by participants. First of all, you should speak with your record keeper about any administrative or other costs, particularly with custom funds. Then, you should have a candid discussion with your record keeper (or whomever handles your employee communication and education program) about their experience with target-date funds. Our direct experience with target-date funds (a span of over ten years), and managed accounts and investment advice (over more than six years) is summarized below.

Overall, Target-Date Funds Have a High Incidence of Improper Use

In our own most recent study on this issue involving a major transit agency and a large state plan, we found that only 24% of the participants in the funds were properly using them (target-date funds). The most common forms of misuse are discussed below. We also know that the findings of our study were not unique. Another major record keeper addressed the same misuse issues during their session at the 2006 NAGDCA conference. While every form of asset allocation or investment advice program is subject to misuse, our findings of improper use by over 70% of participants in the funds is very high. Another study by an independent consulting firm found that as few as 6% of participants in target-date funds invested all of their account in a single target-date fund over time. While every situation can be different, here are the most common issues regarding participant usage of target-date funds:

1. **Changing Funds Based on Return**

   Some participants initially select the proper fund for their estimated retirement age with assistance during the enrollment process. Because participants have been conditioned to look at fund returns, however, some participants regularly examine the rates of return of the various funds. For example, one of the large target-date fund vendors currently shows a one year return for the 2040 fund to be nearly 11% while the rate of return on their 2010 fund is just under 8.50%. When participants begin to compare returns for the target-date funds, there is a temptation to switch to the "best performing" fund.

2. **Participants Select More Than One Fund**

   Having been advised for years to diversify, a fairly high percentage of participants in our study selected more than one target-date fund based on that premise, or they selected a target-date fund *and* a couple of their "favorite" funds as well.

3. **Selecting the Wrong Fund for Their Personal Circumstances**

   We previously discussed the fact that most pre-packaged target-date funds are designed for the corporate 401(k) market, and not governmental plans. However, another inherent problem with target-date funds is that the participant may have lifestyle plans that mean they should not be in a fund targeted to the date they plan to "retire". In addition, they may have outside assets or income from other sources, such as a spouse or partner, that, when taken into account, would indicate that their own funds should be invested more aggressively (or more conservatively) than a fund targeted on their age. Our own education counselors have repeatedly pointed out this issue with target-date funds, and as a consequence, they spend a disproportionate amount of time trying to assist the participant in selecting the "right" target-date fund without providing investment advice.

4. **Public Safety**

   The retirement options available to public safety personnel, as well as their other unique circumstances, makes the selection of proper target- date funds even more arduous. The ability to retire earlier would, on the one hand, indicate that the selection of a target-date fund for a public safety employee should be "stepped-back" from the age range in the target-date fund to reflect their own, earlier retirement date. However, the situation becomes even more complex because many public safety employees who "retire" from public service with one employer often go on to a second career. This means that even the original target dates in target-funds may be inaccurate given the fact that these employees may leave funds invested for many more years before beginning to withdraw them after their (assumed) "retirement date".

5. **Governmental Defined Benefit Plans Are A Key Element Ignored by Target-Date Funds**

   If a plan sponsor opts to create custom target-date funds it is possible to ask your manager to take into account the fact that virtually all of the participants in the defined contribution plan have a defined benefit income during retirement. However, if the plan sponsor utilizes pre-packaged target-date funds, these funds are generally not managed with that in mind. While some consultants think this can be solved by adding several years to your expected retirement date (so the participant selects a more aggressive target-date fund), this process can be confusing for participants. We have seen something as simplistic as saying "if you are a government employee pick a target-date fund that is ten years beyond your anticipated retirement date".

   While it might make sense for many participants to invest their defined contribution plan assets more aggressively if they have a defined benefit plan, imagine the confusion among your participants when you tell them they need to "age adjust" their target-date fund selection to get them into the portfolio that is better for them. Worse yet, issuing those types of recommendations to plan participants could be interpreted as providing investment advice. The simple fact is that the "dating" in pre-packaged target-date funds may be inappropriate for governmental employees who usually are covered under a defined benefit plan as well. Managed accounts is the only option that specifically takes into account the projected income from the defined benefit plan, and other household assets, in selecting the optimal portfolio for each participant.

The Managed Accounts Alternative

A well-constructed managed account program offers the following advantages when compared to a balanced fund or target-date fund alternative:

1. Managed accounts is the only option that takes into account the participant's individual circumstances in selecting a portfolio for them, and changing the selection automatically over time. As a default option, the participant receives a higher level of immediate personal attention than either a balanced fund or a target-date asset allocation fund:

   - First of all, the managed account vendor is provided with the participant's age, sex, and other information captured at the time of enrollment. Based on this information, the managed account provider selects a portfolio based on what is known about this participant, and about other similarly situated participants of that same age, sex, etc.

   - The managed account vendor knows other key plan-level information such as whether or not the participant will be covered under a defined benefit plan and/or social security.

   - The managed account vendor is also constructing the portfolios using the core funds in the plan sponsor's plan (and not any other funds not approved by the plan sponsor).

All of this is done upon enrollment, with NO action by the plan participant. When compared to a balanced fund option or target-date fund, the managed account option immediately takes into account all of the above information on the participant before the first portfolio is even selected. While this information is less than the managed account provider would like to ultimately have from each participant, it is far more than utilized by the balanced fund or target-date provider.

This basic amount of information can be significant, even if the participant never provides any more information. For example, a study by another company concluded that adjusting portfolios for the impact of the defined benefit plans produced a gain of 400 basis points in a 12-month period. [11] While we have yet to quantify the difference on our own business, we do observe that this one step alone makes a significant difference in the portfolios created by the managed account provider (presence of a defined benefit plan). Similar adjustments by a balanced or target-date fund would of course be impossible.

2. Shortly after enrollment, and every 12 months thereafter, the managed account provider (the model used by Great-West) contacts the participant and asks for more personal information such as:

    - Other household assets used for investment
    - Retirement objectives and timelines
    - Other sources of retirement income for the participant, or from a spouse, partner, or prior employment of either or both
    - Other key personal information relative to the objectives of the participant for retirement

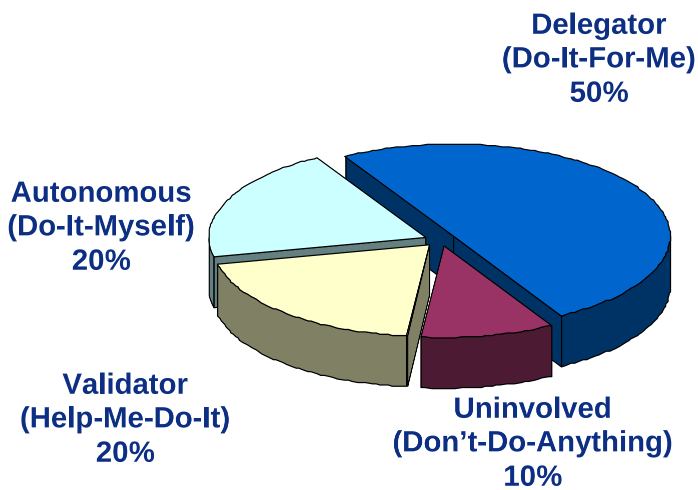
    The above information may be provided in writing, by completing the form sent by the managed account provider, or the participant may call a toll-free number and provide the information to a counselor in a personal conversation.

    This information is used by the managed account provider to adjust the portfolio selection for the participant based on the new, more detailed personal information. The process is updated each quarter, but the participant may call at any time they wish to update their profile, especially when they have a life-changing event like a marriage or birth of a child, etc. In addition, each participant in managed accounts receives a full Annual Review with a summary of their information and how their portfolio has performed over the previous period.

3. With managed accounts, there is no rate of return chasing or participant confusion about what target-date fund to choose. Managed accounts change the focus from return comparison to goal achievement and therefore reduces the desire to chase fund returns.

Our own research indicates that there are four primary behaviors among plan participants in defined contribution retirement plans:

[11] AIG Study



Based on our own research and focus groups among governmental employees, we have found that about more than half of all plan participants want "someone else to do it for me" when it comes to managing their retirement funds. About 20% can use guidance tools and other market information to "do it themselves" and are likely "knowledgeable investors" to some degree. Another 20% are "validators" who can use tools like investment advice to help them validate or re-in force their decisions. In actuality, we have found that the percentage of "delegators" is higher than the 50% or so who describe themselves as such. When managed account services are available along with investment advice and investment guidance, participants tend to select managed accounts overwhelmingly. In fact, as of the date of this writing, based on our own governmental plans, of the participants who make a selection between one of the three services, 96% select managed accounts, 1.7% select advice, and 2.4% select guidance. However, when measured in terms of assets, approximately 70% of assets are in managed accounts, 13% is in investment advice, and 17% in guidance, which reflects the larger account balances among the advice and guidance participants as opposed to managed account participants, who tend to have smaller balances, at least initially.

Interestingly, other studies have found the same behavior classifications among retirement plan participants in their studies. The JP Morgan study referred to earlier classified participants as "40% to 70% are "delegators" – least likely to be actively engaged[12]. Another report emphasized the fact that once they make an initial election at enrollment, most participants do not make an additional asset allocation change - "85% of participants are on allocation autopilot."[13] Our findings have been similar with fewer than 14% of participants in our governmental plans making a trade or rebalancing their funds in the past 12 months.

Finally, when comparing overall plan usage, many plan sponsors with target-date funds find their usage capping out at about 10% of plan assets. A study by an independent consulting firm indicated that usage of target-date funds at the macro plan level has been flat at about 10% for some time and in fact decreased from a high of 15% in 1995.[14] Our experience has shown that the misuse of these funds (discussed earlier) is a primary reason for their lack of long term appeal for most plans. To the contrary, plans where the full suite of investment guidance, investment

[12]" Ready! Fire! Aim? – How some target date fund designs are missing the mark on providing retirement security to those who need it most" a white paper report by JP Morgan, March 20, 2007

[13] Corporate Executive Board Retirement Services Roundtable 2002

[14] Hewitt – In Brief – 401(k) Evolution 06/2005

advice, and managed account services have been offered for two years or more, overall usage is at much higher levels than asset allocation funds.

What About Fees?

As with any other investment option, fees are an important element when considering a QDIA selection. Earlier in this article we mentioned that the balanced fund option may be the least expensive from the standpoint of total fees. Target-date (lifecycle) funds are usually “funds of funds” which means the total fee is a weighted average of the investment management and other fees applicable to the underlying funds, *plus* any fee assessed on the entire fund to provide the asset allocation, rebalancing, glide path, etc. In some situations where the target-date funds are composed 100% of the fund manager’s own proprietary funds, there is no other fee in addition to the fees in the underlying funds. In other situations, particularly for custom target-date funds, the fee ranges from .10% to .40% or more of fund assets to provide the target-date fund management services for each portfolio. When comparing funds, be sure you are looking at a “total” net expense figure that includes all the fees on the underlying funds and fees assessed on the overall fund itself, if any.

Managed account programs are usually (but not always) offered as part of a suite of services that includes investment guidance, investment advice, and managed accounts. In most cases investment guidance is free, and it helps the participant select asset class allocations but not specific funds. Investment advice is usually provided for a flat fee of $25-$75 annually and while it does identify specific funds and an asset allocation, the participant must actively elect the funds and rebalance their portfolio on a regular basis. The managed account option permits the participant to have their account professionally managed, in which case the manager selects the funds, automatically rebalances the portfolios and adjusts the mix of stocks, bonds, and fixed funds in the portfolios as required by age, life events or other conditions specified by the participant. On an individual basis, professional fund management can be 1.00% of assets per annum or more if bought on a retail basis from a brokerage firm or investment manager. For corporate and governmental defined contribution plans, fees are usually half the retail rate, or less. In most situations a “full service” managed account program will start at about .55%-.70% of assets per annum and decrease as assets grow. Most firms offer a sliding scale whereby the fee decreases as assets increase, with final breakpoints as low as .20% or thereabouts. In most cases the average participant will be paying about .50% of assets or less, plus the underlying fund management fees.

Determining the most effective QDIA on a cost/reward basis is quite easy. Balanced funds and target-date funds publish their returns in a manner that can be easily compared over time. In addition, most managed account providers can give you actual results on how well participants in the managed account block have done compared to participants in the plan who do not use the service. While managed account historical performance may not be as long as balanced funds or target-date funds, there is enough historical data from most providers to permit the plans sponsor to make an assessment of which type of QDIA provides the best historical results in terms of return minus cost. In our own analysis, this information was easy to get and fairly easy to assess over reasonable periods. While there is no guarantee of future performance, the historical comparison is a good place to start.

Conclusion

We are not against target-date funds. Our intention in this edition of *Focus on 457* is to summarize our own experience with all three options (balanced funds, target-date funds and managed accounts) over the past ten years, and the issues to consider before offering any of them, particularly as your QDIA selection.

Our own experience thus far clearly indicates that managed accounts have more benefits and fewer drawbacks as a QDIA than target-date funds. Balanced funds have even more problems with a “one size fits all” philosophy than the target-date fund options. This may not be true in every situation, and of course each plan sponsor needs to arrive at their own conclusion on this topic. While there may be reasons to include balanced funds and target-date funds in your investment array, each clearly has disadvantages as a QDIA when compared to managed accounts.

Our own experience with these funds and the research we have conducted, as well as research that was done by others referenced herein has led us to a “best practices” model on this subject:

- Managed accounts are the option that best addresses the issue of providing participants with professional investment management of their defined contribution assets. This suite of services should include investment guidance and advice, but managed accounts is clearly the best (and most utilized option) for the majority of participants who need professional management.

- Ideally, a “best practice” situation would automatically enroll all new employees in the defined contribution plan, and place them in managed accounts. Participants have the option to “opt-out” of the service at the time they are enrolled without paying any managed account fee. The Pension Protection Act of 2006 specifically provides for this as a safe harbor default for automatic enrollment (as it does for a target-date fund or balanced fund). Our experience with this model on a major state plan has been exceptionally positive. *Fewer than 8% of participants opted out of the professional managed account service when automatically enrolled in it at the time of employment.*

- If a plan sponsor opts not to offer managed accounts, then offering target-date funds is the “next best” option. However, there is a big difference in results and potential misuse between managed accounts and asset allocation funds of any type.

- While target-date funds are the current fad, their high incidence of misuse will eventually have to be fixed by the product vendors or the plan sponsors that use them. A complete “fix” of all the various forms of misuse discussed in this article may be quite difficult.

Each plan sponsor must determine which QDIA is best for their plan. As we said at the opening section of this issue of *Focus on 457*, automatic enrollment, and automatic deferral increase are probably the most significant steps you can take to boost the accumulation of retirement savings assets in your plan. To implement such a program, you must select a QDIA, and while none of the QDIA options is perfect each has unique advantages over the traditional “default investment options” most plans are using today. Please refer to the table in the Executive Summary for a side-by-side comparison of the three options.

DC Plans Underperformed DB Funds

By Chris Flynn, Manager Defined Contribution Investment Benchmarking, and Hubert Lum, Research Director, CEM Benchmarking Inc. at www.cembenchmarking.com.

Defined Contribution plans underperformed Defined Benefit funds by a wide margin over a long period—by 1.8% per year over the eight-year period ending in December 2005. On an annual basis, DC plans underperformed DB funds for seven consecutive years, through up and down markets, to 2005. The findings were based on the CEM investment performance databases, which comprised 616 DC plans with total assets of $500 billion and 1,323 DB funds with total assets of $2 trillion. Table 1 shows the performance difference between DC plans and DB funds.

Table 1: Defined Benefit versus Defined Contribution Performance, 1998- 2005			
	Defined Benefit (8-yr avg)	**Defined Contribution (8-yr avg)**	**Difference (DB-DC)**
Total return	7.5%	5.7%	**1.8%**
-Policy return or weighted benchmark return[1]	6.7%	5.1%	**1.6%**
=Gross value added	0.8%	0.6%	**0.2%**
-Costs	0.4%	0.4%	**0.0%**
=Net value added	**0.4%**	**0.2%**	**0.2%**

[1]Policy return was used for DB funds while benchmark returns weighted by asset classes were used for DC plans. Source: CEM Benchmarking Inc.

What is the effect of this 1.8% difference on the DC participant's future account value? At the end of 25 years, the effect is a reduction in that participant's future account value by 34%. The stakes are high so an understanding of the reasons for this underperformance is valuable.

The key driver for the under performance of DC plans was differences in asset mix. Large holdings of under performing GICs, company stock and cash reduced the return of DC participants. This group of assets accounted for 41% of DC plan assets but only 1% of DB fund assets. These assets crowded out better performing asset classes such as foreign stock, real estate and alternative investments. These better performing asset categories made up only 4% of DC plan assets compared with 24% of DB fund assets. Table 2 shows the asset mix differences.

The largest negative impact on DC plan returns was produced by company stock. From 1998 to 2005, the average compound return on company stock was 1.7% compared with 4.8% for the S&P 500 or 6.0% for the Lehman Aggregate Bond Index. Further, the increase in risk through holdings of company stock was noteworthy. Over the eight-year period, the standard deviation in returns for company stock was 38%. This volatility was twice that of the S&P 500.

Table 2: Asset Mix Differences Between Defined Benefit Funds and Defined Contribution Plans, 1998-2005		
Asset Class	**Defined Benefit (8-yr avg)**	**Defined Contribution (8-yr avg)**
Stocks		
Company stock	0%	19%
Large cap	40%	38%
Small Cap	5%	6%
Foreign	16%	4%
Total stocks	61%	67%
Bonds, GICs and cash		
Bonds	30%	10%
GICs	0%	18%
Cash	1%	4%
Total bonds, GICs, and cash	31%	32%
Other assets		
Real estate	4%	0%
Alternatives	4%	0%
Total other assets	8%	0%

Source: CEM Benchmarking Inc.

While DC plan sponsors do not invest participant assets, they have several levers to influence participant asset mix. The place with perhaps the greatest potential to influence participant asset mix is the default option. Behavioral finance suggests that participants are likely to leave their contributions in the default option because of inertia. CEM research has shown that assets in an investment option, when designated as the default, were 2.3 times higher than assets in the same option when it was not the default.

Therefore, if a DC plan sponsor wants the asset mix of its participants to resemble the asset mix of a DB fund, then the DC plan sponsor should use a balanced fund option as the default option. However, Table 3 shows that the most common default options for most funds in the CEM database were GICs, stable value and cash.

Table 3: Type of Default Option in 2005	
	% of Total
GICs/stable value/cash	**53%**
Balanced funds	**34%**
Other	**13%**

Source: CEM Benchmarking Inc.

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Table 4: Matching Programs in 2005	
	% of Total
Cash	**64%**
Company stock	**31%**
Both	**5%**

Source: CEM Benchmarking Inc.

Another important driver of the DC participant asset mix is the matching option. Again, if the intention is make the DC plan look more like a DB plan, then the DC sponsor should match with a balanced fund option or with cash and a balanced fund default. However, Table 4 shows that 31% of plans still match employee contributions with company stock.

The final key driver of the DC participant asset mix is the investment options offered. This influences the DC plan participant asset mix in two ways. First, if an asset class is not offered, participants cannot invest in it. Table 5 shows that a large proportion of funds in the CEM database failed to offer several important asset classes.

Table 5: Plans Not Offering Key Asset Classes in 2005

	% of Total
Real estate and REITs	84%
TIPS	92%
Alternatives	99%

Source: CEM Benchmarking Inc.

Table 6: Investment Options in 2005

	Median Number
Company stock	1
Domestic stock	6
Foreign stock	2
Bonds	1
Balanced funds	3
GICs/stable value/cash	1
Other	1
Total	15

Source: CEM Benchmarking Inc.

Second, investment options influence asset mix based on the "1/n" behavioral finance rule. This rule describes naïve diversification whereby a participant allocates contributions evenly among the n investment options offered by the DC plan[i].

This may partly explain the low bond holdings of the average DC plan asset mix relative to the average DB asset mix. Table 6 shows that, in 2005, the average DC plan had 15 investment options but, typically, only one of these was a bond option. It is not surprising then that investments in this important DB asset class were relatively small.

[1] Shlomo Benartzi and Richard Thaler, "Naïve Diversification Strategies in Defined Contribution Saving Plans," The American Economic Review 91.1 (2001): 79-98.

FINAL IRS REGULATIONS—NORMAL RETIREMENT AGE AND IN-SERVICE DISTRIBUTIONS

By: Mary Beth Braitman, Terry A. M. Mumford, and Lisa Erb Harrison of ICE MILLER, LLP

Generally. On May 22, 2007, the IRS issued final regulations regarding distributions from pension plans upon attainment of normal retirement age prior to a participant's severance from employment with the employer maintaining the plan. Treas. Reg. § 1.401(a)-1(b). These regulations finalized the portion of the proposed phased retirement regulations relating to normal retirement age and in-service distributions upon attainment of normal retirement age. (The portion of the proposed phased retirement regulations which would have permitted in-service distributions before normal retirement age under a bona fide phased retirement program have not been finalized.) A pension plan that is subject to these final regulations includes a defined benefit 401(a) plan or a defined contribution 401(a) plan that is not a 401(k) or profit sharing plan. For example, a number of public employers have established a defined contribution plan to accept employer matching contributions to employee deferrals to a 457(b) plan or 403(b) tax-sheltered annuity. Plans that would not be subject to the final regulations include 401(k) plans, profit sharing plans, 457(b) deferred compensation plans, and 403(b) tax-sheltered annuities.

In-Service Distributions. The final regulations clarify that a pension plan may be designed to permit payment of benefits upon an employee's attainment of normal retirement age, even if the employee has not yet had a severance from employment with the employer maintaining the plan. This is consistent with the language included in the proposed regulations, as well as the existing practice among some pension plans based on earlier IRS guidance (such as Revenue Ruling 71-24). In-service distributions are not required to be included in the plan design.

Normal Retirement Age. However, the final regulations differ from the proposed regulations in defining a permissible normal retirement age under a pension plan. The proposed regulations had provided that a normal retirement age could not be set so low as to be a "subterfuge to avoid the requirements of section 401(a)" and, thus, could not be "earlier than the earliest age that is reasonably representative of a typical retirement age for the covered workforce." In response to comments expressing some reservations about this standard, the final regulations replace the subterfuge standard with a requirement that "<u>the normal retirement age under a plan must be an age that is not earlier than the earliest age that is reasonably representative of the typical retirement age for the industry in which the covered workforce is employed</u>." Treas. Reg. § 1.401(a)-1(b)(2).

Normal Retirement Age Safe Harbor—Age 62 or Older. The final regulations provide a "safe harbor" for a plan with a normal retirement age of age 62 or older, which is deemed to be not earlier than the earliest age that is reasonably representative of the typical retirement age for the industry in which the covered workforce is employed. This safe harbor is based on Internal Revenue Code ("Code") Section 401(a)(36), as added by the Pension Protection Act of 2006 ("PPA"). Code Section 401(a)(36) provides that, for plan years beginning after December 31, 2006, a pension plan does not fail to qualify under Code Section 401(a) solely because the plan provides that a distribution may be made to an employee who has attained age 62 and who has not separated from employment at the time of the distribution.

Normal Retirement Age—Under Age 62 But Not Earlier Than Age 55. Under the final regulations, if a pension plan's normal retirement age is earlier than age 62, but not earlier than age 55, the determination of whether the normal retirement age "works" (is not earlier than the earliest age that is reasonably representative of the typical retirement age for the industry in which the covered workforce is employed) is based on all of the relevant facts and circumstances. In the preamble to the final regulations, the Treasury Department states that, if the normal retirement age is between the ages of 55 and 62, it is generally expected that an employer's good faith determination of the typical retirement age for the industry in which the covered workforce is employed will be given deference, assuming that the determination is reasonable under the facts and circumstances. However, this normal retirement age range is not a safe harbor under the final regulations.

Normal Retirement Age—Under Age 55. If a normal retirement age under a pension plan is lower than age 55, the age is <u>presumed to be earlier</u> than the earliest age that is reasonably representative of the typical retirement age for the industry in which the covered workforce is employed, unless the Commissioner determines otherwise based upon the facts and circumstances.

Normal Retirement Age Safe Harbor—Qualified Public Safety Employees. Given the typically earlier retirement ages for public safety employees, for a pension plan where substantially all of the participants are "qualified public safety employees" (within the meaning of Code Section 72(t)(10)(B), as added by the PPA), a normal retirement age of age 50 or later is deemed not to be earlier than the earliest age that is reasonably representative of the typical retirement age for the industry in which the covered workforce is employed. Under Code Section 72(t)(10)(B), a "qualified public safety employee" means "any employee of a State or political subdivision of a State who provides police protection, firefighting services, or emergency medical services for any area within the jurisdiction of such State or political subdivision."

Part-Time Employment. The final regulations state that a reduction in hours does not constitute a retirement. Therefore, in-service distributions are not permissible prior to normal retirement age in the case of a reduction in hours worked. Treas. Reg. § 1.401(a)-1(b)(3).

Effective Date. The final regulations are generally applicable May 22, 2007. However, for governmental plans, the regulations regarding normal retirement age and part-time employment apply with respect to plan years beginning on or after January 1, 2009. Collectively bargained plans may have a different effective date.

Impact. These final regulations may have a significant impact for sponsors and administrators of defined contribution plans (other than 401(k) and profit sharing plans) that permit in-service distributions or who are considering the addition of such distributions under their plans. Plan sponsors and administrators will need to consider whether the safe harbors under the final regulations provide sufficient flexibility for their membership, or whether their actual retirement patterns would better align with the use of a normal retirement age outside the safe harbors that would need to be supported under the stated IRS standards. It is important to realize that implementation of the final regulations may require a plan language amendment.

WASHINGTON REPORT

By: Susan J. White and Jonah Mainzer, Susan J. White and Associates, Inc.

Legislative Update: U.S. Senate and House of Representatives Introduce Companion National Save for Retirement Resolutions!

As Washington settles into the heat of summer, the 110th Congress moved forward on the NAGDCA supported National Save for Retirement Week by passing companion resolutions on June 20, 2007.

In follow up to the successful passage of the Resolution in the fall of 2006, Senator Smith (R-OR), once again took the lead, and Senator Conrad (D-ND) joined him in crafting the Resolution (S. Res. 240) and introducing it in the Senate. S. Res. 240 establishes the week of October 21, 2007 as National Save for Retirement Week. Both Smith and Conrad are members of the Senate Committee on Finance and are active members on retirement and pension related matters. Smith is also the top Republican member of the Senate Special Committee on Aging and Conrad chairs the Senate Committee on the Budget.

The House joined this effort with Representative Schwartz, (D-PA) and Representative Sam Johnson (R-TX) introducing a companion resolution, drafted and supported by the House Committee on Ways and Means—the House tax-writing committee. Both Schwartz and Johnson are members of Ways and Means which has jurisdiction over governmental defined contribution plans. The Committee has worked closely with Senators Smith and Conrad in drafting the Resolution and in working out the many legislative process issues in order to move forward jointly. A goal of both Ways and Means and the Senators has been to pass the Resolution this summer in order to give the public and private sectors plenty of time to plan events for National Save for Retirement Week.

Building on the positive nationwide response in October 2006 to National Save for Retirement Week, NAGDCA has worked closely with the Senate and House in order to ensure passage this year of the Resolution and further the goal of educating and urging employees—both public and private—to increase their savings for retirement. In addition to seeking this critical recognition from Congress, NAGDCA has also been working with both chambers to begin an effort that would create legislation authorizing a permanent Savings for Retirement Month.

The Committee on Ways and Means, working closely with Senators Smith and Conrad, plans to begin the process of drafting a bill this summer. Once passed by the House and Senate, the legislation would go to the President for a Savings for Retirement Month proclamation.

Washington has Full Agenda

In the meantime, Congress and the White House remain embroiled in the debates surrounding the Iraq war, executive privilege, the continuing investigation of the Department of Justice activities, immigration and energy legislation. In addition to these pressing matters, Washington must also address the budget and how to finance the government for the coming year.

Over the last few weeks the House and Senate Committees on Appropriations have begun the process of resolving the budget for fiscal year 2008 and these bills are sure to be as contentious as they have been in previous years—with the President issuing another warning that he will veto spending bills that are not to his liking. Last year most of the appropriations bills funding the federal departments, except for Defense and Homeland Security were never even passed. Subsequently, the government has been funded this year under a Continuing Resolution, maintaining all funding at last year's levels.

In addition to struggling with these broader based issues, Congress has continued its interest in a number of pension related matters, including the administrative fees and other fees charged by defined contribution plans. Numerous bills have been introduced in this Congress—many focused on automatic IRAs and generally aimed at expanding defined contribution options.

Congress Continues Oversight of Defined Contribution Administrative Fees

The first hearing held by the House Committee on Education and Labor—the Committee charged with oversight of ERISA—focused predominantly on private 401(k) plans and disclosure. Education and Labor is also crafting legislation, due to be introduced sometime this summer, that aims to address disclosure and conflicts of interest. The measure is due to be introduced sometime this summer.

In addition to Education and Labor, the House Committee on Ways and Means Oversight Subcommittee is planning a yet-to-be announced hearing for the end of June. In this first hearing, the Committee plans to focus on views from the federal agencies, including the Department of Treasury (DOT), the General Accounting Office (GAO) and the Securities and Exchange Commission (SEC). The SEC announced this spring that it plans to work with the Department of Labor to develop guidelines related to disclosure of fees.

Both the Senate Committee on Finance and the Senate Committee on Health Education, Labor and Pensions (HELP) have indicated their interest in fees, however nothing specific, at this time has been pursued. Once the Senate dispenses with some of the other broad-based issues facing it, such as immigration, energy legislation and reauthorization of health coverage for children, there could be movement on this front.

Older Workers Legislation: NAGDCA to Participate on Kitchen Cabinet Advising Senator Smith on Bill

In addition to the numerous bills introduced in both the Senate and House this year addressing various aspects of the retirement funding puzzle, Senator Smith is working on legislation focused on women and older workers.

Senator Gordon Smith (R-OR)—Senate sponsor of Savings for Retirement Week and member of the Senate Finance Committee and the Senate Special Committee on Aging is in the process of crafting legislation to address older workers and phased retirement issues. He has formed an advisory kitchen cabinet that includes representatives from both the public and private sectors, including NAGDCA. The first meeting is scheduled for the end of June.

Smith is interested in expanding the eligibility of the Work Opportunity Tax Credit (WOTC) to allow the credit for employers hiring older workers; improving the Workforce Investment Act for older workers; updating the minimum required distribution rules in a number of ways, including raising or indexing the age at which minimum distributions must begin; removing the penalty under the Civil Service Retirement System for part time services.

The Senator is considering a number proposals to address long term care insurance needs, including allowing tax-free distributions to participants from defined contribution plans to purchase qualified long-term care insurance. He is also proposing to create a National Resource Center on Aging and the Workforce to serve as a national clearinghouse on older workers and workforce issues that include solutions affecting planning for older workers that would serve employers, community and government organizations and public and private agencies.

Women's Retirement Security Act of 2007 (S. 1288)

On May 3, Senator Smith reintroduced the Women's Retirement Security Act. This bill had originally been introduced at the end of the 109th Congress, but as no action was taken it had to be reintroduced this year. The bill would increase retirement savings through automatic IRAs, expansion of access to IRAs expanding the Saver's Credit, and Flexible Savings Account transfers for public and private employees.

There are also provisions to preserve income, including incentives for lifetime payments, study of spousal consent for distributions from defined contribution plans and longevity insurance.

The Department Treasury Issues Letter Clarifying Guidance on Pension Protection Act Public Safety Worker Provision

In response to congressional inquiries, the Department of Treasury (DOT) sent a letter to Congress on May 15, 2007 stating its intention to include self-insured plans in the definition of qualified health insurance premiums under § 845 of the Pension Protection Act of 2006. The administrative position will soon be included in a formal announcement. Until then, DOT clarified that funds can begin using the May 15 letter to implement the Health and Long Term Care Insurance for Public Safety Officers (HELPS) benefit.

NAGDCA, along with numerous other pubic interest groups, had sought clarification of the provision after DOT issued original guidance which did not include self-insured plans in the definition of qualified health insurance premiums. NAGDCA's Executive Board met with Treasury officials and with congressional committees and offices in February where the issues were discussed.

Technical Corrections

The Congressional tax-writing Committees—House Ways and Means and Senate Finance—have indicated that a technical corrections bill on the Pension Protection Act of 2006 (Public Law 109-280) would be introduced this year. Originally, both the House and Senate discussed the possibility of introducing technical corrections legislation in the spring or early summer. Although the Committees have been working with the Department of Treasury and the Joint Committee on Taxation, legislation has not yet been introduced.

The key task facing lawmakers is keeping the bill narrow and technical in nature under pressure to expand the legislation to address broader policy issues, including the defined benefit provisions of the 2006 Pension Protection Act. With the public safety workers health insurance provision now addressed by Treasury, there is no longer a push for a technical correction, removing some momentum for the measure.

Congress Pursues Interest in Roth 457

In late March, as Congress debated supplemental funding for the Iraq War, the Senate added tax legislation to the first of such bills that included a provision creating a Roth 457. The Senate Committee on Finance crafted the provision, however, the tax provisions were dropped from the overall legislation. It is unclear, at this time, whether the provision will move forward this year.

During the February 2007 Executive Board meeting in Washington, the Board added support for a Roth 457 to NAGDCA's federal legislative agenda and discussed the issue during the Board's annual congressional and DOT visits.

AROUND THE COUNTRY

NAGDCA To Award Member of Media With 2007 Media Recognition Award

NAGDCA is currently accepting nominations for its 2007 Media Recognition Award. Nominations are due on July 13, 2007 and can be submitted online at http://www.nagdca.org/media/media_award.cfm. This annual award is presented to a member of the media for outstanding coverage of pension and retirement issues in newspapers, magazines, national newsletters or research reports.

"NAGDCA established the Media Recognition Award in 2001 as a way of recognizing members of the media that do a great job of covering the government defined contribution industry," says Ralph Marsh, NAGDCA President. "Public sector plans have unique features that are often misunderstood and NAGDCA believes it is important to recognize the efforts of the media to clearly and accurately report our issues."

Nominations may be made by media publishers and/or reporters, or directly from the NAGDCA membership. The award is given for a specific article or outstanding cumulative coverage over the fiscal year, July 1, 2006 to June 30, 2007. NAGDCA members and the members of the media have been encouraged to submit published articles or reports that they believe have been particularly effective in discussing issues or concepts related to retirement issues generally and/or administration of defined contribution plans that relate to state or local governments and their employees.

The 2007 award will be presented at this year's annual conference which is being held September 15 – 19, in Indian Wells, CA.

NAGDCA's 2nd Webcast for 2007 will highlight the use of Target Date Funds within Defined Contribution Plans

The National Association of Government Defined Contribution Administrators, Inc. (NAGDCA) has opened registration for NAGDCAST #2 on Target Date Funds withing Defined Contribution Plans. This upcoming webcast, scheduled for July 17, 2007 at 1:00 p.m. EDT.

Confirmed speakers include: Moderator, Ed Lilly, State of New York Deferred Compensation Program; Georgette Gestely, New York City, NY; Keith Hocter, Bellwether Consulting; John Poth, State of Texas; Kandi Hicks Winters, State of Florida. The webcast will cover aspects of implementing target date funds into state and local government defined contribution plans. These funds were designed to make retirement investing easier. For many plans they have succeeded in doing so, but there are considerations that must be taken when researching, evaluating and implementing these funds into a retirement plan. This webcast has been geared to provide an in-depth look at target date funds and how they are evaluated for certain plans. The panelists will be sharing their experiences on evaluating fund options; working with and without consultants; implementing target date funds; and educating and promoting these funds to participants.

Registration for *NAGDCAST #2: Target Date Funds* is free for government members and $100.00 for non-members. More than 200 participants are expected to participate.

The PowerPoint presentation for *Target Date Fund* webcast will be available at www.nagdca.org by 11:00 am EDT the morning of July 17. Register at www.nagdca.org (*Latest News* section, in the middle of the homepage) or by going directly to: https://nagdca.on.raindance.com/confmgr/event_register.jsp?eventId=43729&invitationId=867159. Advance registration is required prior to the start of the event.

NAGDCA Member Benefit Spotlight

To remind members of benefits they receive that they may not be aware of, we will be spotlighting a benefit of membership in each edition of *The Contributor*. For more information on this or any benefit of membership, please visit our website at http://www.nagdca.org/ or contact NAGDCA staff at (859) 514-9161.

Annual Conference
Every year NAGDCA holds its annual meeting in different locations throughout the country. The conference is central to the association's purpose. Sessions during the meeting focus on specific aspects of federal law, investments, communication and administration within /defined contribution/deferred compensation. Each conference provides timely information to all association members and the opportunity to hear nationally recognized speakers. The meeting also provides members the chance to discuss deferred compensation issues with peers from other state and local governments, as well industry providers. The conference is only open to current NAGDCA members; non-members are not able to attend.

2007 Annual Conference
September 15 - 19
Indian Wells, California
Hyatt Grand Champions Resort and Spa

New Members

Please visit the NAGDCA on-line directory for member's full contact information. You will need a username and password to access the information.

NAGDCA State Government Primary Member
John Fisher
State of West Virginia Treasurer's Office

Steve Kerns
State of West Virginia Consolidated Public Retirement Board

Christine Rackers
Missouri State Employees' Retirement System (MOSERS)

NAGDCA Local Government Primary Member
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Barbara Mollo
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NAGDCA Government Secondary Member
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Tulare County

Ray Bullick
Tulare County

Rick Dah
Missouri State Employees' Retirement System (MOSERS)

Lori Disbrow
City of Jersey City

Gary Findlay
Missouri State Employees' Retirement System (MOSERS)

Endeliza Hampton
City of Oakland

Dave Kehler
Tulare County

Scott Simon
Missouri State Employees' Retirement System (MOSERS)

Karen Stohlgren
Missouri State Employees' Retirement System (MOSERS)

Vicki Sutton
State of West Virginia Consolidated Public Retirement Board

Paula Van Horn
State of West Virginia Consolidated Public Retirement Board

Rita Woodard
Tulare County

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New York University

Benjamin Taylor
Harvard University

Sharla Taylo
Texas Tech University

Scott Ungaro
Texas Tech University

ABOUT THE CONTRIBUTOR

The Contributor is published quarterly by the National Association of Government Defined Contribution Administrators, Inc. (NAGDCA). NAGDCA encourages the submission of articles on topics relating to defined contribution/ deferred compensation retirement savings/plans. Articles that appear under the by-line of an individual express the opinions of the author and not those of NAGDCA as an organization. The deadline for submissions for the next issue is October 12, 2007. Articles should be approximately two pages in length and should be submitted in Word format. Please direct all newsletter items and questions to NAGDCA, 201 East Main Street, Ste. 1405, Lexington, KY 40507. You may also e-mail submissions to Robert Hansel at rhansel@AMRms.com. Please contact Robert Hansel at 859-514-9161 with any questions or comments.

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