Mercer

welcome to brighter

Defined Contribution Plan Sponsor

Quarterly Update

2Q 2023

A business of Marsh McLennan

Defined Contribution Quarterly Update Webinar

Speakers

Kelly Henson (Moderator)
US Defined Contribution
Investment Strategy Leader

Rhonda Berg
Senior Defined
Contribution Consultant

Brian Kearney
Principal,
Law & Policy Group

Geoff Manville
Senior Director,
Government Relations

1. DC landscape at a glance
2. Judicial updates
3. Legislative & regulatory updates
4. Trending topics

DC landscape at a glance

‘ESG Rule’ experiences multiple challenges and Presidential support

Form 5500 Changes … audited financials, MEP/PEPs, and more

DB plans are taking advantage of interest rates, may shift more assets to DC plans.

Cybersecurity
GAO recommends DOL provide more guidance

Retirement Readiness post COVID

Navigating capital preservation in a rising interest rate environment

Inflation and market volatility hit retirement confidence

Judicial updates

1

Judicial update

Litigation and enforcement

Cases by the numbers for Q1 2023[1]

Cases closed

14 settlements
$55.3 Million

18 dismissals

Cases by key theme

1 managed accounts	29 fees and investments	8 403(b) plan/ not-for-profit	4 operations

5 target date funds	1 recordkeeper	2 proprietary funds	1 stock/ESOP	1 NQDC

[1] Information sourced through Law360, Pensions & Investments, NAPA and PlanSponsor as of April 24, 2023.
Cases listed represent some recent litigation and are not intended to be a complete representation.

Judicial update

Litigation and enforcement

Recent areas of focus

- Reasonableness of recordkeeping fees
- Reasonableness of investment management fees (mutual fund share classes vs. collective trusts vs. separate accounts)
- Mismanaging plan operations
- Appropriateness and performance of funds offered, including target date funds
- Offering proprietary investments
- Appropriateness of managed account program fees and services

List represents some recent trends and is not meant to be a complete representation.

Excessive fee litigation – key developments

Northwestern revisited

- Supreme Court decided on case in January 2022, disagreeing with Seventh Circuit's dismissal, remanded case
- Seventh Circuit decided in March 2023 that two of the three claims should go back to district court[1]:
  - Failure to monitor recordkeeping fees
  - Failure to use institutional over retail share class investments

Yale heads to trial

- Case originally filed in August 2016, and after some history, judge reached a split decision in October 2022, allowing breach of fiduciary duty claims to proceed to trial[2]:
  - Failure to monitor and avoid unreasonable recordkeeping fees
  - Failure to obtain competitive recordkeeping bids
  - Use of asset-based pricing
  - Failure to prohibit TIAA from cross-selling to participants
- Unless settlement is reached, jury of citizens will decide ERISA excess fee imprudence case for the first time[3]

Uncertainty remains for future of excessive fee litigation

Mercer GRIST: 7th Circuit revives excessive fee claims after high court ruling (Apr. 25, 2023)

[1]New Hughes v. Northwestern Decision Could Mean More Litigation, Plansponsor, April 9, 2023

[2]Yale 403(b) Fiduciary Breach Counts Withstand Motions, Plansponsor, October 31, 2022

[3]Yale Hospital Must Face Trimmed ERISA Excessive Fee Suit, Law360, March 3, 2023

Legislative and regulatory updates

2

Congress focused on SECURE 2.0 fixes, increased oversight

Partisan fight over debt limit, federal spending not yet affecting retirement policy

- House GOP bill cuts IRS funding, Biden budget wants curbs on Roth conversions, cap on tax-preferred savings
- Retirement-related revenue raisers will continue to be attractive to both parties

Work on SECURE 2.0 corrections bill continues, timing uncertain

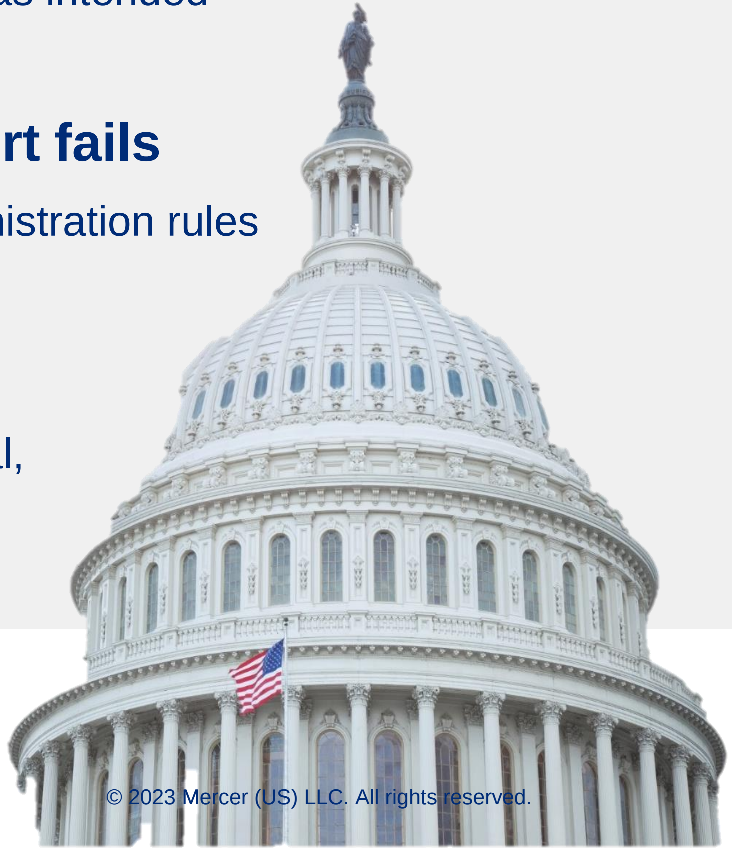
- Lawmakers discussing implementation issues with regulators, who may enforce law as intended
- Bipartisan legislation would permit 403(b) plans to invest in collective trusts

Final ESG investment rule safe for now as Republican repeal effort fails

- GOP bills continue to target plan investments; Democrats seek to codify Biden administration rules

Increased House oversight activity may spotlight concerns about DOL agenda

- ESG rule, fiduciary definition, Qualified Professional Asset Manager (QPAM) proposal, cybersecurity may be targets



SECURE 2.0 agency guidance outlook

Will agencies prioritize guidance based on a provision's effective date or statutory deadline?

2023

- Option to offer Roth election for matching and nonelective contributions
- Increased age for required minimum distributions (RMDs)
- Reliance on participant's self-certification for hardship distribution eligibility
- Distributions for terminal illness
- Relaxed rules for lifetime income options, including QLACs
- Simplified disclosures for unenrolled participants
- Overpayment recovery rules

2024

- Matching student loan payments
- Mandatory Roth catch-up contributions for high earners
- Distributions for personal emergencies and domestic abuse
- Pension-linked emergency savings accounts
- Starter 401(k) plans
- *Blended performance benchmarks for asset allocation funds*
- *Expanded self-correction under EPCRS*
- *Retirement Savings Lost and Found*

2025

- Long-term part-time worker eligibility rules
- Mandatory auto-enrollment for most new plans
- Higher catch-up contribution limit at ages 60-63

2026

- Distributions to pay for qualified long-term care insurance premiums
- Annual paper statement requirement

Items in italics are agency deadlines.

Mercer Law & Policy Group GRIST articles on SECURE 2.0

- Implementing SECURE 2.0's Roth provisions may tax DC plan sponsors (April 11, 2023)
- Taking a closer look at SECURE 2.0's penalty-free distribution provisions (***updated*** March 13, 2023)
- User's Guide to SECURE 2.0 (***updated*** March 7, 2023)
- Taking a look at SECURE 2.0's defined benefit plan provisions (Feb. 21, 2023)
- Road-testing SECURE 2.0's auto-enrollment mandate for new DC plans (Feb. 14, 203)
- SECURE 2.0 brings more changes to required minimum distribution rules (Feb. 7, 2023)
- Alert: SECURE 2.0 retirement reforms set to become law (Dec. 20, 2022)

ESG regulatory update

Department of Labor (DOL) Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights

Mar. 10, 2021

DOL announced a non-enforcement policy on regulations on investment selection and proxy voting finalized late in 2020.[1]

Oct. 14, 2021

DOL proposed amendments to 2020 rule to specifically allow consideration of material ESG factors, but agency also suggested fiduciaries may often be required to consider ESG factors.

Dec. 13, 2021

Public comment period closed. DOL received more than 895 written comments and 21,469 petitions (e.g., form letters).[2]

Nov. 22, 2022

DOL released pre-publication of final rule.

Dec. 1, 2022

DOL published final rule in the *Federal Register*.

GRIST: On second thought, DOL has softer touch with ESG investing rule (Dec. 13, 2022)

Jan. 26, 2023

25 state attorneys general and 3 plan participants filed suit in Texas federal court to stop the rule from taking effect.

Jan. 30, 2023

Most provisions in the final rule took effect.

Feb. 21, 2023

2 plan participants filed a second lawsuit in Wisconsin federal court to block the final rule.

March 1, 2023

US Congress passed a bill to overturn ESG final rule.

March 20, 2023

President Biden vetoed the bill that would have overturned the final rule.

Dec. 1, 2023

Two provisions from the final rule related to proxy voting will take effect.

[1] Financial Factors in Selecting Plan Investments & Fiduciary Duties Regarding Proxy Voting and Shareholder Rights.
[2] Source: 2022-25783.pdf (federalregister.gov)

Updated Form 5500

Applies starting with 2023 plan year filings

Optional DC group filing	SECURE 1.0 created a group filing option for DC plans that have the same trustee, named fiduciary, plan administrator, plan year and investment options.
Schedule H changes	Schedule H, *Financial Information*, will have 11 categories of administrative expenses (increased from 4 categories).
New Schedule MEP	All MEPs — including PEPs, association retirement plans and professional employer organization (PEO) plans — will use Schedule MEP to report information currently required to be reported in an attachment.
Change to IQPA audit threshold	Large-plan audit requirement will be determined by the number of participants with account balances at the beginning of the plan year (instead of the number of eligible participants).
IRS compliance questions	Plans will need to report whether they pass minimum coverage and nondiscrimination tests using permissive aggregation. 401(k) plans will also need to indicate if they're a safe harbor plan, and if not, if they use prior-year testing for ADP and ACP tests.

Mercer GRIST: Form 5500 trilogy concludes with latest set of changes (March 13, 2023)

IRS auditors looking at plan loan offsets

A **plan loan offset** occurs when a portion of a distribution that's otherwise payable to a participant is used to pay off the participant's outstanding plan loan.

A **qualified plan loan offset (QPLO)** is a plan loan offset that occurs when the distribution is triggered by the participant's severance from employment or the plan's termination.

Both types of loan offsets are actual distributions that **can be rolled over** to another employer plan.

Regular 60-day rollover deadline applies, except **QPLO rollover deadline is extended** to the participant's tax filing deadline (with extensions) for the year in which the offset occurs.

Mercer GRIST: IRS snapshot focuses on plan loan offsets (April 2, 2023)

IRS audit focus

- Has the participant had a permissible distribution event?
- If the participant was still employed when the offset occurred, does the plan allow in-service distributions?
- Was the participant eligible for the extended QPLO rollover deadline?
- Did the plan properly report the plan loan offset on the Form 1099-R?

IRS proposed regulations on use of forfeitures

Extended deadline to use forfeitures

Current rule:
Deadline is end of the plan year in which forfeitures arise

Proposed rule:
Deadline is 12 months after the end of the plan year in which the forfeitures arise

Permitted uses for forfeitures

Paying administrative expenses

Reducing employer contributions, including restoring unrecovered overpayments

Increasing benefits in other accounts, including ADP/ACP corrective contributions

Plan documents must state the deadline for using forfeitures and how they will be used.

The regulations would be effective for the 2024 plan year, but plans can rely on the new rules now.

Mercer GRIST: IRS proposal would clarify the rules for retirement plan forfeitures (March 28, 2023)

Trending topics

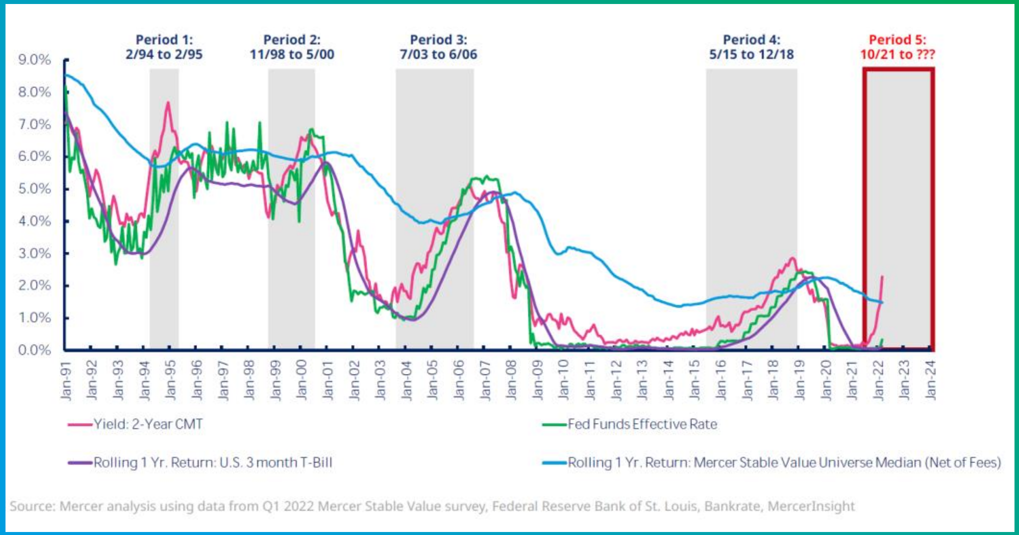
3

Stable value in a rising interest rate environment

A viable long-term option, despite rough seas in the near future

- **Market-to-book (MV/BV) ratios will decline as interest rates are rising.**
  - Potential for some managers to drop below 95% MV/BV. Some managers have the ability to temporarily employ a modified crediting rate formula to increase MV/BVs more quickly
- **Wrap capacity remains healthy and wrap providers understand the potential trajectory of MV/BVs.**
  - Investment guidelines are more conservative compared to the Global Financial Crisis and wrap providers are willing to work with stable value managers through a challenging rate environment.
- **Put queues and cash flows are important.**
  - Managers with a shorter put queues and strong cash inflows are likely to fare better (dilution of MV/BV shortfall and greater reinvestment opportunity). Stable value managers rated highly by Mercer currently exhibit healthy cash flow profiles.
- **Stable value ultimately benefits from rising rates, but with a delay.**
  - Stable value managers are able to **reinvest** at lower bond prices and **higher yields**, ultimately improving return potential.

Analysis of Rising Rate Environments



Gray bars highlight rising rate environments as defined by when either the Fed started raising interest rates, or when the 2 Year CMT rose significantly in anticipation of a Fed rate hike.

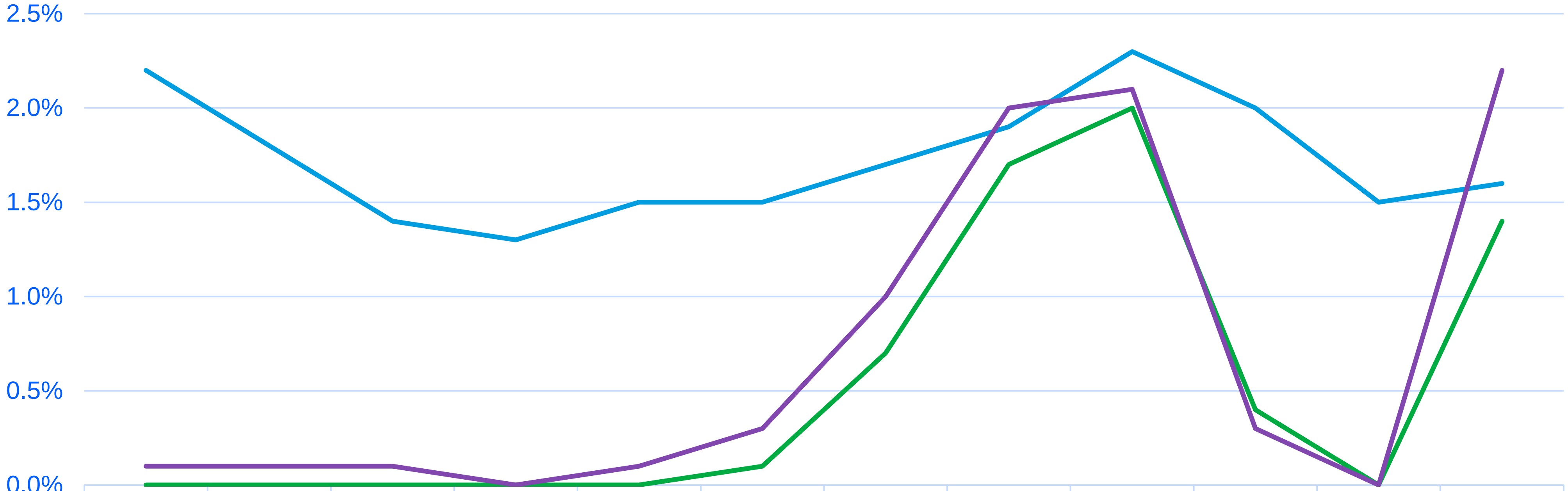
While money market fund yields increase at a faster pace (U.S. 3 month T-bill) compared to stable value (Mercer Stable Value Universe Median) during rising rate environments, money market outperformance has historically been short-lived.

[Mercer Paper: Stable Value in a Rising Rate Environment]

Why not money market?

Historical Median Returns: Return in $US (after fees) over last 12 calendar years ending December 2022

Our research shows that the guarantee of principal and accumulated interest, combined with the historically higher returns could make stable value through a security backed investment contract more attractive, despite some of the liquidity restrictions.



	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Stable Value Median	2.2%	1.8%	1.4%	1.3%	1.5%	1.5%	1.7%	1.9%	2.3%	2.0%	1.5%	1.6%
Money Market Median	0.0%	0.0%	0.0%	0.0%	0.0%	0.1%	0.7%	1.7%	2.0%	0.4%	0.0%	1.4%
3-Month T-Bill	0.1%	0.1%	0.1%	0.0%	0.1%	0.3%	1.0%	2.0%	2.1%	0.3%	0.0%	2.2%

Source: Mercer Insight

Retirement confidence is down

EBRI 2023 Retirement Confidence Survey

#1 Reason for lack of confidence among workers is lack of savings, followed by inflation concerns

47% Of workers say debt is negatively impacting their ability to save

84% Of workers report increased cost of living will make it harder to save

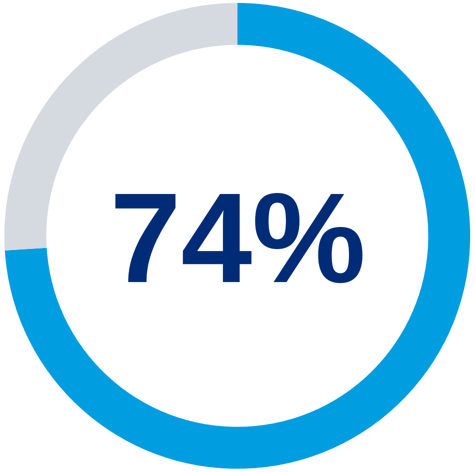
Only 64% of workers feel confident they will have enough money in retirement, down from 73% in 2022.

Source: EBRI 2023 Retirement Confidence Survey.

Mercer

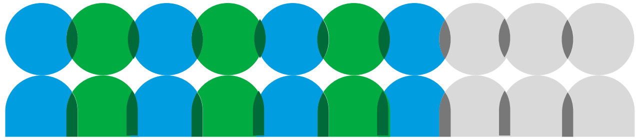
Participants investment behaviors and concerns in 2022

EBRI 2023 Retirement Confidence Survey



Of workers worry the stock market will be increasingly volatile

16% of workers switched to more conservative investments in their workplace retirement plan in 2022



7/10 **Workers are confident they can pick the right investment options for their situations.**

However, there are major gaps in investment option familiarity and notable education opportunities around investments.

4/10 participants don't understand target date funds

3/10 participants don't understand managed accounts

5/10 participants don't understand ESG

Source: EBRI 2023 Retirement Confidence Survey.

Responding to Retirement Confidence & Participant Behaviors

EBRI 2023 Retirement Confidence Survey

Assessing your participant needs and demographics is key before considering any actions below.

Responding to Inflation Concerns

- Consider adding inflation sensitive investment options, like diversified real asset funds, if not already offered
- Education around inflation protection options already available, may be beneficial

Responding to Debt Concerns

- Evaluate what budgeting tools or debt consolidation opportunities are available
- Assess SECURE 2.0 provisions that might help with emergency savings, or matching structures that provide flexibility (e.g. matching on student loan debt)

Recordkeeper updates

- Empower[1] and TIAA[2] join Portability Services Network, LLC, a consortium of recordkeepers in coordination with Retirement Clearinghouse, LLC
- Empower begins Prudential recordkeeping migrations[3]
- T. Rowe Price completes acquisition of Retiree, Inc., a retirement income planning fintech firm[4]

[1]Empower Joins Fidelity, Vanguard and Alight in Portability Consortium, Plansponsor, Februrary 13, 2023

[2]TIAA Joins Major Recordkeepers in Portability Services Network, Plansponsor, April 4, 2023

[3]https://www.empower.com/prudential-migration

[4]T. Rowe Price Completes Acquisition of Retiree, Inc., Cision PR Newswire, April 20, 2023

Automatic Portability Services Network

- Fidelity Investments, Vanguard, Alight Solutions, Empower, and TIAA announced a consortium of workplace retirement plan recordkeepers, Portability Services Network, LLC (“PSN”) with Retirement Clearinghouse, LLC (“RCH”)
- Low account balances for terminated participants can be forced out which requires participants to pay taxes and penalties and participants with low-account balances often take lump sums rather than establishing an IRA or rollover to new employer’s plan
- Clearinghouse for automatically locating a terminated participant’s small balance account (less than $5,000) from a former employer’s retirement plan to an active account at new employer’s plan when a participant changes employment
  - Both plan sponsors required to enroll in auto portability service with a participating recordkeeper
  - RCH is program’s fiduciary, sends consent notices upon a match in the active account; money is transferred and invested according to current participant’s investment elections or the plan’s QDIA
  - Participants pay one-time fee when an account balance is matched and transferred to active account

Key Benefits

- Preserves retirement savings
- Makes portability easier
- Removing small balances increases average account balance
- Reduces lost participants, uncashed check issues

Key Considerations

- Fiduciary responsibility for engaging service providers
- Due diligence should be performed:
  - Plan compliance, regulatory requirements
  - SECURE 2.0 impact
  - Sharing of participant data, data security
  - Compensation and fees
  - Plan sponsor reporting
  - Participant experience

Important notices

References to Mercer shall be construed to include Mercer LLC and/or its associated companies.

This contains confidential and proprietary information of Mercer and is intended for the exclusive use of the parties to whom it was provided by Mercer.

This content may not be modified, sold or otherwise provided, in whole or in part, to any other person or entity without Mercer's prior written permission.

Mercer does not provide tax or legal advice. You should contact your tax advisor, accountant and/or attorney before making any decisions with tax or legal implications.

This does not constitute an offer to purchase or sell any securities.

The findings, ratings and/or opinions expressed herein are the intellectual property of Mercer and are subject to change without notice. They are not intended to convey any guarantees as to the future performance of the investment products, asset classes or capital markets discussed.

Past performance is no guarantee of future results. The value of investments can go down as well as up, and you may not get back the amount you have invested. Investments denominated in a foreign currency will fluctuate with the value of the currency. Certain investments, such as securities issued by small capitalization, foreign, or emerging market issuers, real property, and illiquid, leveraged (including through the use of derivative instruments), or high-yield funds, carry additional risks that should be considered before choosing an investment manager or making an investment decision.

Mercer universes: Mercer's universes are intended to provide collective samples of strategies that allow for peer group comparisons over a chosen timeframe. Mercer does not assert that the peer groups are wholly representative of and applicable to all strategies available to investors. One cannot invest directly in a Mercer universe.

For Mercer's conflict of interest disclosures, contact your Mercer representative or see http://www.mercer.com/conflictsofinterest.

This does not contain investment advice relating to your particular circumstances. No investment decision should be made based on this information without first obtaining appropriate professional advice and considering your circumstances. Mercer provides recommendations based on the particular client's circumstances, investment objectives and needs. As such, investment results will vary and actual results may differ materially.

Information contained herein may have been obtained from a range of third party sources. While the information is believed to be reliable, Mercer has not sought to verify it independently. As such, Mercer makes no representations or warranties as to the accuracy of the information presented and takes no responsibility or liability (including for indirect, consequential, or incidental damages) for any error, omission or inaccuracy in the data supplied by any third party.

Investment management and advisory services for U.S. clients are provided by Mercer Investments LLC (Mercer Investments). Mercer Investments LLC is registered to do business as "Mercer Investment Advisers LLC" in the following states: Arizona, California, Florida, Illinois, Kentucky, New Jersey, North Carolina, Oklahoma, Pennsylvania, Texas, and West Virginia; as "Mercer Investments LLC (Delaware)" in Georgia; as "Mercer Investments LLC of Delaware" in Louisiana; and "Mercer Investments LLC, a limited liability company of Delaware" in Oregon. Mercer Investments LLC is a federally registered investment adviser under the Investment Advisers Act of 1940, as amended. Registration as an investment adviser does not imply a certain level of skill or training. The oral and written communications of an adviser provide you with information about which you determine to hire or retain an adviser. Mercer Investments' Form ADV Part 2A & 2B can be obtained by written request directed to: Compliance Department, Mercer Investments 99 High Street, Boston, MA 02110.