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# Segal Study of Multiemployer Defined Contribution Plans

Turmoil in the markets and compliance with the Pension Protection Act of 2006 have put multiemployer defined benefit (DB) plans in the spotlight in recent years. However, multiemployer defined contribution (DC) plans, which are usually designed as a supplemental retirement benefit, are also an important — if secondary — source of retirement security for participants. To better understand the characteristics of multiemployer DC plans, The Segal Company conducted a study in late 2008. This brief report summarizes the results of the *Segal Study of Multiemployer Defined Contribution Plans*, which reflects information for just under 140 funds, all but two of which are Segal clients. The study sample represents 9 percent of all multiemployer DC plans.[1] As a group, the DC plans in the study cover more than 600,000 lives and have more than $15 billion in assets.

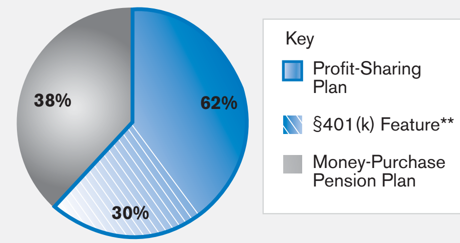
## DC Plan Offerings

An overwhelming majority of the DC plans in the study (82 percent) are companions to DB plans sponsored by the same unions and contributing employers for the same active workers. Dual coverage (under both DB and DC plans) is much less common in the single-employer arena. For example, a recent survey by the International Foundation of Employee Benefit Plans (IFEBP) found that just under 32 percent of employers offer both a DB and a DC plan.[2]

"An overwhelming majority of the DC plans in the study... are companions to DB plans."

As shown in Graph 1, most of the multiemployer DC plans in the Segal study — 62 percent — are profit-sharing plans. Before 1987, there were few, if any, multiemployer profit-sharing plans, because employers could only contribute to those plans out of current or accumulated profits. Leaving the basis for contributions in any given time period to an employer-by-employer determination of profitability was not tenable for multiemployer plans where retirement plan contributions are negotiated as part of the overall wage and fringe package. After the Tax Reform Act of 1986, which eliminated the need to have actual profits in order to contribute to a profit-sharing plan, multiemployer profit-sharing plans began to proliferate. Growth in the number of multiemployer profit-sharing plans reflect both the creation of new plans and the conversion of money-purchase plans to profit-sharing plans because profit-sharing plans are simpler to administer than money-purchase plans and can include Section 401(k) features.

**Graph 1: Plan Type***




* None of the funds in the study offered more than one type of DC plan.

** This slice of the pie chart represents the portion of profit-sharing plans that have §401(k) features.

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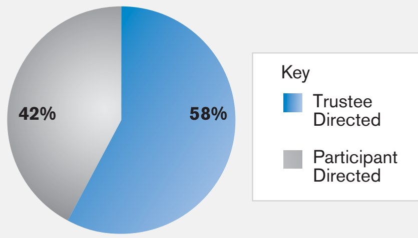
The number of multiemployer profit-sharing plans has grown even though one of the most attractive features of profit-sharing plans for corporations — the fact that the employer can reserve discretion over whether and how much to contribute — is irrelevant for multiemployer contributors. Their contribution obligation is fixed in a collective bargaining agreement, so that the participants' rights to the contributions are not affected by the profit-sharing designation. Almost 30 percent of the profit-sharing plans in the study allow voluntary, salary-reduction participant contributions through a §401(k) feature.

[1] According to *Private Pension Plan Bulletin: Abstract of 2006 Form 5500 Annual Reports* (http://www.dol.gov/ebsa/pdf/2006pensionplanbulletin.pdf), published by the Department of Labor's Employee Benefits Security Administration in December 2008, there are 1,530 multiemployer DC plans in the U.S.

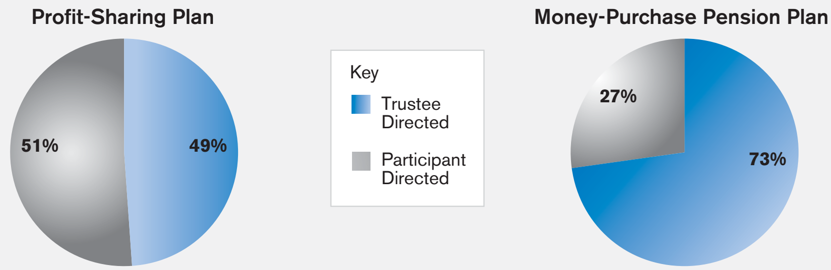
[2] The IFEBP *Employee Benefits Survey: U.S. and Canada 2009* also found that half of employers only offered a DC plan. Just under 14 percent offered no retirement plan and 4 percent only offered a DB plan. A 2006 publication from Boston College's Center for Retirement Research (http://crr.bc.edu/images/stories/Briefs/ib_50.pdf?phpMyAdmin=43ac483c4de9t51d9eb41) reported that the percentage of workers covered under both a DB and DC plan (not necessarily from the same employer) was 28 percent in 2004, according to Department of Labor data, or 17 percent that same year, according to data from the *Survey of Consumer Finances*.

### Graph 2: Direction of Investments*




* One of the DC plans in the study is partially trustee directed and partially participant directed. It is excluded from this graph.

### Graph 3: Direction of Investments by Plan Type*




* One of the DC plans in the study is partially trustee directed and partially participant directed. It is excluded from this graph.

## Investments

Although trustees direct investments for more than half of the DC plans in the study (58 percent), a large percentage of the plans (42 percent) allow participant-directed investments. See Graph 2 above.

Graph 3 at the top right of this page shows the breakdown of how investments are directed by plan type. The study suggests that participant-directed plans are almost three times more likely to be profit-sharing plans than money-purchase pension plans.

The study gathered information about which service providers were used by the 55 plans that offer participant-directed investments. Information was obtained for all but two of those plans. A total of 14 service providers were represented.

As Graph 4 below shows, no service provider dominates, but roughly half of the plans in the study use one of three providers in the proportions shown. The text box on the last page discusses state-of-the-art DC plan administration.

The study found that annual account valuations are most common, performed by 55 percent of the multiemployer DC plans represented. At the other end of the spectrum, just under one-third of the multiemployer DC plans studied perform daily valuations. Graph 5 on the bottom of page 3 shows these results, as well as the percentages of plans that value accounts monthly and quarterly.

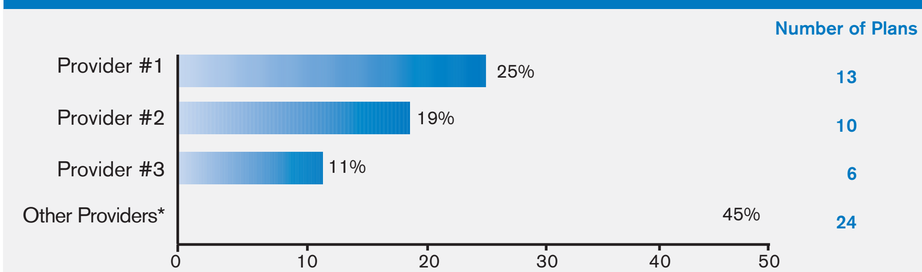
Since the study was conducted, many boards of trustees of plans with annual account valuations have changed their plan provisions to value accounts more frequently to reflect investment performance more accurately at the point of distribution.

The study did *not* collect information about the investment performance of the assets of DC plans with different characteristics.

## Provisions for Early Withdrawals

Under the Internal Revenue Code, money-purchase pension plans are prevented from making in-service distributions including hardship withdrawals, although they are allowed to have loan provisions. Profit-sharing plans are permitted to allow in-service distributions as well as loans, although §401(k) accumulations attributable to pre-tax employee contributions can only be withdrawn in case of hardship by someone still working for the employer.[3]

### Graph 4: Service Providers Used by Plans with Participant-Directed Investments




* This group represents 11 other providers. A total of 14 service providers were represented.

[3] Converting a money-purchase pension plan to a profit-sharing plan involves careful administration. The trustees would be required to issue an ERISA Section 204(h) notice to all plan participants because the contributions are no longer guaranteed by law, even though they may be guaranteed by the collective bargaining agreements. Moreover, if the plan wants to take full advantage of the withdrawal flexibility allowed for a profit-sharing plan, it would need to maintain separate accounting for the contributions (and earnings thereon) made before and after the conversion. Hardship withdrawals would be limited to contributions and assets received after the conversion date. ***As with all issues involving the interpretation of laws, trustees should rely on their fund counsel for authoritative advice.***

"Trustees direct investments for more than half of the DC plans in the study."

Hardship withdrawals are limited to distributions due to medical expenses, costs related to the purchase of a primary residence or to prevent eviction, certain educational expenses, funeral expenses and certain expenses related to the repair of damage to the participant's primary residence. The distribution must be necessary to satisfy the financial need and may not exceed the amount of the need, which may include any federal, state or local income taxes or penalties.

Loans are limited to the lesser of $50,000 or 50 percent of the vested account balance. Loans also present administrative challenges for plans, especially in situations when — as with multiemployer plans — repayments cannot be made through payroll deduction.

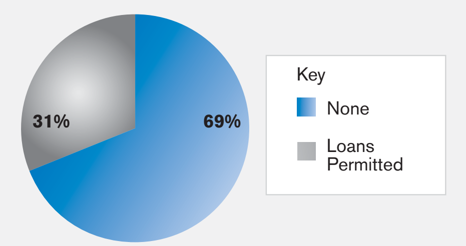
It is not surprising then, that the study found that loans and hardship withdrawals are relatively uncommon. Approximately one-third of the multiemployer DC plans in the study offer those provisions: 31 percent for loans (see Graph 6) and 35 percent for hardship withdrawals (see Graph 7). Since the study was conducted, many boards of trustees of DC plans that did not allow hardship withdrawals have begun to reevaluate this decision in light of the severity of participants' economic problems.

"The study found that loans and hardship withdrawals are relatively uncommon."

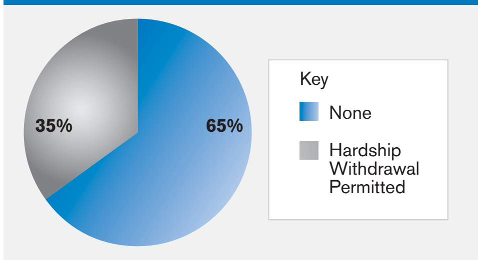
## Payment Options at Retirement

A large majority of the multiemployer plans in the study (83 percent) offer payment options in addition to lump sums. See Graph 8. These include monthly installments, a combination of a partial lump sum and monthly installments, and a lifetime annuity (either a lifetime annuity for the participant or a husband-and-wife annuity). Money-purchase pension plans require an annuity option.[4]

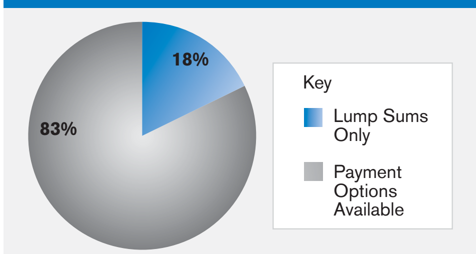
**Graph 6: Loan Provisions**




**Graph 7: Hardship-Withdrawal Provisions**

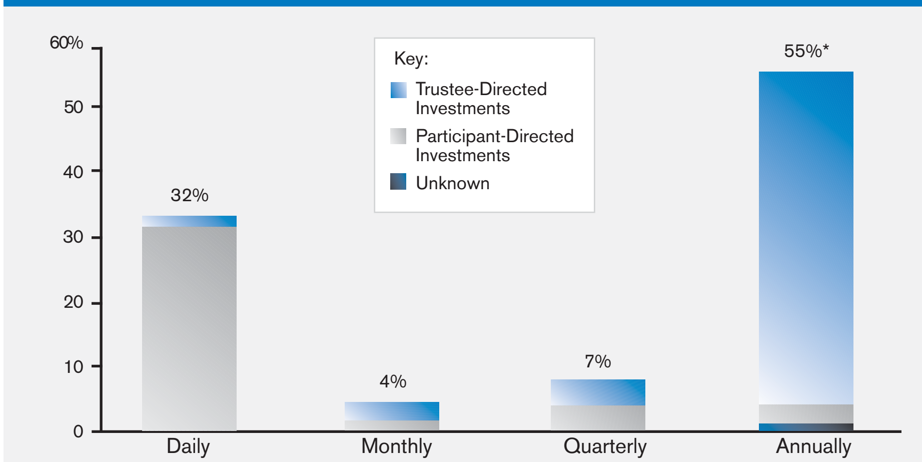



**Graph 8: Account Payments***




* Total exceeds 100% due to rounding.

**Graph 5: Frequency of Account Valuation**




* The total of the participant-directed and trustee-directed segments for DC plans with annual valuations does not equal 55% because information about investment direction was not available for three of those plans (2.19%).

## Conclusion & Commentary

The *Segal Study of Multiemployer Defined Contribution Plans* confirmed that multiemployer DC plans are primarily offered as long-term savings opportunities to supplement

[4] As with defined benefit plans, contributions made to a money-purchase plan and the earnings on those contributions must be paid out as a single life or husband-and-wife annuity unless rejected by the participant and spouse (if any). This is true for the money-purchase account even after the plan is converted to profit sharing for future contributions.

### State-of-the-Art DC Plan Administration

When hiring a service providers for a DC plan, trustees should look for the following:

- Service provider commitment to the multiemployer market,
- Dedicated member service center to multiemployer plans,
- Participant-friendly communications/education services,
- Open architecture for investment options, and
- Full disclosure of all fees.

Once a DC plan provider is hired, managing the relationship entails:

- Establishment of performance standards,
- Development of ongoing communications/education plan,
- Service provider attendance at periodic trustee meetings, and
- Independent ongoing review of administrative services and investment options.

*This information was provided by Segal Advisors, the SEC-registered investment consulting affiliate of The Segal Company. Segal Advisors offers an organized process for vendor selection and plan implementation called DC-Connect®. For more information about Segal Advisors or DC-Connect, visit www.segaladvisors.com or contact Robert A. Liberto at 212.251.5324 or rliberto@segaladvisors.com.*

companion DB plans. Historically, DC plans have allowed participants to use the accumulated account balances as a hedge against inflation and the erosion of the value of their DB pension plans' monthly benefit. This is currently being challenged by economic conditions. Nevertheless, because of the supplemental relationship of multiemployer DC plans to DB plans, it is likely that in most cases participants in multiemployer DC plans can wait to improve the asset levels in their DC plans, which will happen over time. It will be interesting to see whether there is a resurgence of interest in and appreciation for traditional DB plans, which protect participants from investment losses and, except in rare instances, have historically been able to back up their commitment to provide a lifetime annuity for benefits accrued to date.[5]

## Outlook

Sponsors of DC plans are likely to soon have to comply with new disclosure requirements. Although the regulations on participant fee disclosures that the Department of Labor proposed during the Bush Administration may not be implemented under the Obama Administration, there is still considerable interest in Washington in requiring DC plan sponsors and vendors to be more transparent.[6] Legislation to require more disclosure has already been introduced in Congress.

In the current climate, trustees of multiemployer DC plans may want to:

- Communicate with participants about what the current economic environment means relative to their defined contribution plan and the companion defined benefit plan,
- Evaluate the need to add loan and hardship-withdrawal provisions,
- Revisit the frequency of account valuation,
- Review investment related issues such as asset allocation options (if trustee directed), and the number and type of funds offered (if participant directed) and
- Assess vendor relationships including services provided and fees charged.

■ ■ ■

*Segal Company consultants and actuaries can be of assistance with the design and communication of multiemployer DC plans. For assistance, contact your Segal consultant or David B. Brenner at 617.424.7330 or dbrenner@segalco.com.*

*Segal Advisors, Segal's SEC-registered investment consulting affiliate, can be of assistance with DC plan investment options, whether they are trustee-directed or participant-directed. For more information, visit www.segaladvisors.com or contact Robert A. Liberto at 212.251.5324 or rliberto@segaladvisors.com.*

[5] For information about the enduring importance and appeal of multiemployer DB plans, see Segal's 2007 *Viewpoint*: http://www.segalco.com/publications/2007viewpoint.pdf

[6] Segal Advisors, The Segal Company's SEC-registered investment consulting affiliate, has prepared a publication on this subject, February 2009 *Segal Advisory*, "Fee Disclosure for Self-Directed Multiemployer Defined Contribution Plans," which is available on the following Web page: http://www.segaladvisors.com/publications/feb09segaladvisory.pdf

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