Plan Sponsor

voice

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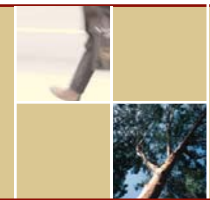

In this issue

Looking Ahead to 2005

Congress is back in session and President Bush has announced an aggressive agenda that includes both Social Security reform and an overhaul of the nation's federal tax system. In regard to Social Security, the Administration has stepped up their campaign to gain popular and Congressional support for a proposal that would allow employees to invest a portion of their Social Security payroll tax in private, or personal, accounts. Specific details about how this would be accomplished were not released at the time of publication.

As to tax reform, on January 7th President Bush announced his appointees to a new commission to explore ways to simplify the federal tax code. Two former Senate tax-writers, Republican Connie Mack of Florida and Democrat John B. Breaux of Louisiana, were named as chair and vice chair. The commission is expected to report its findings to the Treasury by July 31, 2005.

As always, Nationwide will be closely monitoring federal legislative and regulatory activities throughout the year. Watch for updates on initiatives that may impact your plan in our Federal Legislative and Regulatory Reports that are issued around the 20th of each month via e-mail and posted on www.nrsforu.com.

Redemption Fees ...Working Towards Uniformity and Simplicity

The mutual-fund industry scandal is now nearly 18 months old. What began as the New York Attorney General's investigation into rogue practices by a few traders has now stretched into other areas that depend on, but have little control around, the mutual fund industry.

Nationwide Retirement Solutions supports efforts to prevent excessive trading activity that may harm long-term investors. We have implemented certain tracking mechanisms and restrictions to deter market timers. The mutual fund industry, however, is adopting a position that the application of redemption fees may do more to control excessive traders.

While increasing participation is a priority of plan sponsors and the retirement industry, the potential for more fees - even if few participants are likely to trigger them - works against efforts to encourage eligible workers to enroll.

Nationwide has discussed the issue of redemption fees with many government plan sponsors. Their reaction has been to work toward simple and consistent application of these fees. "Keeping it simple" will reduce or eliminate confusion and help participants understand why these fees have been instituted and how they can protect their long-term investments.

Because many deferred compensation plans offer a spectrum of investment options from several fund families, uniform application of redemption fees is extremely important.

Over the next several months, Nationwide will be introducing a series of redemption-fee measures that, coupled with trading restrictions, will assist in protecting plan assets from excessive trading activity. Key to our success is continued communication with, and cooperation of, plan sponsors.
If you have any questions about this effort, please call your Nationwide Plan Representative.

Plan Design and its Impact on Employee Participation

Should governmental employers worry about low participation in their supplemental deferred compensation plans?

Most governmental 457 plans, on average, have a participation rate of between 30% and 50%. The higher percentage is typically dependent on certain plan design features, such as an employer matching contribution.

But deferred compensation plans are supplemental to their employer-sponsored pension system, right? So does this lower participation really matter? This article explores why supplemental plans are increasing in importance and how plan design can make a difference in employee participation rates.

Retirement Income Gap

The percentage of pre-retirement income that is needed to maintain an individual's standard of living during retirement is increasing. Several years ago, the general standard was around 60%. More recently, this amount has been expressed as a range between 60% and 80% of pre-retiree income. Studies[1], however, are showing that this percentage is increasing each year, with the latest data suggestion that the replacement ratio should be between 75% and 89%–the higher percentage being needed for employees with annual incomes that are $50,000 or lower.

What this means is that the gap between income that results from primary retirement benefits (pension plus Social Security, if available) and the level of income that will be needed to support a comparable retirement lifestyle is also increasing. Many public employees continue to believe that employer benefits (i.e., pension, retiree health plans, Social Security) will take care of them in retirement. Employees often don't realize that they will likely have an income gap between what they need to support their retirement lifestyle and their primary benefits.

A few changes in a public employer's supplemental plan design can improve employee chances for a financially successful retirement. The following discusses the plan features and their impact on participation rates in defined contribution plans.

Plan Design

A report entitled *Plan Design and 401(k) Savings Outcomes*[2] (the Report) explored how plan features can impact employee participation. The Report focused on private sector 401(k) plans but parallel comparisons can be made to government sector defined contribution plans. The following discusses five different features in the Report that have an impact on participation rates.

Automatic (negative) enrollment - Most plans require an affirmative election to defer into a defined contribution plan. However, the Report findings showed that there are drastic increases in employee participation if they are automatically enrolled in the plan, unless they "opt out". This has the greatest impact on low tenure employees, with a 50% increase in participation for those with less than five years of employment.

This negative election approach has drawbacks, however, as the deferral contribution rate and investment selection is defaulted to a common choice determined by the employer. Often employees retain these predetermined choices and fail to take action to increase deferrals or select different investment options that may be more appropriate for their personal long-term needs.

Active decision enrollment - With an active decision enrollment, employees are required to sign an election form indicating their decision to enroll in the defined contribution plan, or not, within a specified time period after hire. The Report findings showed a marked increase (28%) using an active choice approach for new hires after three months of employment.

Active decision requirements are often applied in the public sector environment for other employee benefits, such as health or life insurance plans. These are rarely, if ever, used for the deferred compensation plan. This easy alternative to the more controversial negative election option (as there are no default choices selected by the employer) could have a significant impact on participation rates as it makes new hires consciously think about their choice to defer and requires them to take action, one way or the other, about this employee benefit.

Employer match - It's no news that an employer matching contribution (based on an employee's voluntary contribution) can have a tremendous impact on participation rates. It has been well documented in several research studies (e.g., *America's Retirement Voice, Public Sector Retirement - Yesterday, Today and Tomorrow). The 401(k) Savings Outcomes Report* findings identified that an employer match increases the probability of employee participation in the plan and the likelihood that the employee will start investing earlier. The dollar amount of the match, or increasing the match value once it has been offered, is less a factor. ***(continued on page 3)***

[1] *AON Consulting 2004 Replacement Ratio Study™*

[2] *Plan Design and 401(k) Savings Outcomes, written for the National Tax Journal Forum on Pensions, June 2004; by James Choi and David Laibson, Department of Economics, Harvard University and Bridgette Madrian, Department of Business and Public Policy, University of Pennsylvania Wharton School*

New Look at www.nrsforu.com

Last December, Nationwide Retirement Solutions launched a new, improved look to the Web site at www.nrsforu.com. The enhancements were based on input received from employers and participants, along with an in-depth evaluation of how the site is currently being used.

The site's home page has a new look that is both inviting, with new colors and layout, and informative, with messages that change frequently to match other participant communications (e.g., newsletters, payroll stuffers, flyers and posters). The secure log-on is now located on the home page so that participants and employers can immediately gain access to their personal or plan accounts with one click.

The site has also been reorganized so that employers and participants can more easily locate information, education and tools. *For example, on the employer site:*

- Legislative and regulatory activity have their own tab at the top of the page to take employers to monthly legislative reports, where the past twelve months issues can be accessed, along with current updates and alerts.
- The Nationwide Retirement Education Institute[sm] has a separate link from the *Employer* page on the right side under *Other Resources,* where research studies and reports are located.
- The current and past issues of *Plan Sponsor Voice* newsletters can now be found on the *Employer Services* page, under *News Bulletins*.

As you use our enhanced Web site, let us know what you think. Your input is important to help us continue to meet the needs of public sector employers and participants. Send an e-mail with your comments to nrsforu@Nationwide.com or contact your Nationwide Plan Representative.

Plan Design and its Impact *(continued from page 2)*

Public sector employers often find it difficult from a budget and political standpoint to offer a matching contribution in their employee benefits package. As state and local governments continue to deal with tight budgets and increasing health care costs, enhancing supplemental retirement plans are often a low priority. But should they be? Encouraging employees to take more personal responsibility in planning for their retirement future can be accomplished through even a very small (e.g., $120 a year) employer match.

Menu of investment options - Many previous studies have shown that there is a correlation between the number of investment choices that employees are offered and participation rates. Offering too many choices can result in employees not taking action because they are confused by the slate of investments. The Report found that increasing the number of investments can actually cause a decline in participation rates.

To address this finding, public sector employers may wish to consider this factor when deciding to increase their investment line-up. Structuring investment spectrums to allow participants to easily evaluate choices and limiting the number of options could make a significant difference in the number of employees who participate in the deferred compensation plan. For example, lifestyle or lifecycle options allow participants to choose one fund based on risk or time horizon. This simplifies the selection for those who are overwhelmed by so many choices in asset classes.

Loans - The Report noted that research conducted by the United States General Accounting Office (GAO) showed that making loans available in a 401(k) plan increased participation by 6%. It was inconclusive, however, as to if this increase was based solely on the plan offering a loan or if other plan features had an impact.

Public sector 457 plans are now eligible to adopt loan provisions but few have actually incorporated these into their plan design. Many plan sponsors are concerned that participants will use these assets for short-term purposes, thus impeding their ability to secure sufficient income for retirement. Based on annual 401(k) plan statistics, however, relatively few participants take advantage of loan options available from their retirement account.[3]

Conclusion

Public sector employers need to take an active role in promoting their supplemental deferred compensation programs to help employees understand their importance in securing a financially successful retirement. There are several design features that can have a positive impact on participation rates. Plan sponsors may wish to explore whether any of these approaches could be incorporated into their deferred compensation plan to encourage and motivate more employees to actively plan for their retirement future.

[3] *EBRI/ICI Participant-Directed Retirement Plan Data Collection Project showed 18% of participants eligible for a loan from their 401(k) plan had an outstanding loan balance at the end of 2003.*

IRC Contribution and Benefit Maximums

Maximum Annual 457(b) Deferral Increases to $14,000 for 2005.

The IRS, Social Security Administration and the Department of Health and Human Services recently published the 2005 contribution and benefit limits. The following table summarizes some of the new limits for 2005 compared to those in effect for 2004. A more comprehensive summary can be found in the November *Legislative and Regulatory Report* at www.nrsforu.com.

Type of IRC Limitation	2005	2004
Pre-tax elective contribution limits for 401(k) and 403(b) plans	$14,000	$13,000
Pre-tax deferrals to 457(b) plans	$14,000	$13,000
Age 50 catch-up contribution maximums under Section 414(v) to 401(k), 403(b), 457(b) plans	$4,000	$3,000
Defined benefit maximum - 415(b)	$170,000	$165,000
Defined contribution maximum - 415(c)	$42,000	$41,000
Annual compensation limit - 401(a)(17)	$210,000	$205,000
Annual compensation limit for grandfathered participants in governmental plans which followed 401(a)(17) limits (with indexing) on July 1, 1993	$315,000	$305,000
Traditional and Roth IRA contribution limits	$4,000	$3,000
Age 50 catch-up limit for Roth and Traditional IRAs	$500	$500

Nationwide Tsunami Donations Near a Quarter-Million Dollars

As a leading insurance company, Nationwide is in the business of helping people return their lives to normal. Immediately after news of the extent of the tsunami damage became clear, the Nationwide Foundation set up a special fund to accept employee and retiree donations–contributions to be matched by Nationwide itself. On Jan. 31, 2005, Nationwide announced that it is forwarding a check to the United Way International's South Asia Response Fund totalling more than $245,000.

But our company's responses to tragedy are more than corporate. They're personal, involving direct involvement. Our employees are often seen on the front lines of relief efforts following hurricanes, tornados, floods and other natural disasters. *Nationwide is on your side.*

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