Wealth Management

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Your Challenge, Our Solutions™

# How to keep employees contributing to the plan

## Here are some steps that employers can take to keep their employees contributing to their retirement plans.

For many employers, especially smaller ones, introducing a retirement plan is a big undertaking. Despite the numerous administrative and regulatory requirements that an employer retirement plan entails, many employers remain committed to their retirement plans because they want to help their employees begin the journey to retirement readiness.

Unfortunately, plan participants can sometimes feel squeezed financially and find it hard to sustain their original commitment to saving for their own retirement security. All too often, other competing and more immediate demands are made on their income, forcing them to reduce or suspend contributions to their plans. While it can be disheartening for employers to see participation rates drop off and contribution levels fall, there are steps they can take to keep employees contributing to their retirement plans. Here are some ideas worth considering.

## Take a fresh look at your plan

Would employees participate more and contribute at higher levels if your plan offered or increased matching contributions? Would a more generous vesting schedule encourage higher participation rates? Would offering a plan loan program have any impact? It can be helpful to reassess and review the way your plan is structured to see how it could become more attractive to employees.

## Focus on regular communications

Use every available platform—live meetings, webinars, emails, intranet articles, etc.—to highlight all the benefits of plan participation. When you reach out to your employees regularly, your messages should always affirm that:

- Plan participants can reduce the income taxes they currently pay when they contribute to their tax-deferred retirement plan.
- Participants do not have to pay income tax on pretax contributions or on any income their contributions might earn until they withdraw money from the plan.
- Contributions in a tax-deferred retirement account can potentially compound more quickly than savings in a taxable account.
- Employer matching contributions are an extra benefit—essentially a bonus that stops when a participant stops contributing to the plan.

## Remind participants that Social Security may not be enough

Social Security retirement payments are a safety net. They help retirees pay their most basic expenses. The

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reality is that most people will have to save for retirement if they want to maintain a standard of living in retirement that is similar to the one enjoyed while working. There really isn't an alternative—and an employer-provided retirement plan is one of the best retirement saving options available.

## Educate participants on the impact of halting contributions

It can be helpful to illustrate for participants exactly how the growth of their retirement plan assets could be affected if they stop contributions—even for a short time. They need to understand that temporarily discontinuing plan contributions can come at a high cost.

## Help employees toward financial literacy

Trying to pay off student loans, saving for that first home, or setting money aside for a child's college education can leave little left over from the average person's paycheck. There's little question that the competing financial demands of modern life can be a struggle for most people. However, plan participants need to believe that it is possible to set aside money for retirement and save for other short- and long-term goals. There are financial education resources and tools available that help people budget, manage debt and lay the groundwork for financial wellness. Your plan's investment managers or recordkeeper may have these resources available.

**Talk with your financial professional. Together, you can develop a strategy to encourage your employees to keep participating in your company's retirement plan.**

# Considering a Roth 401(k)?

### Sponsors should know these rules and requirements before adding a Roth 401(k) option to their plans.

The Roth 401(k) option is becoming increasingly popular with plan sponsors. What general rules and requirements should sponsors know about when considering to add this feature?

## Benefits of a Roth 401(k)

Although traditional 401(k)s and Roth 401(k)s have many similarities, they also have many important differences. With a traditional 401(k), participants make retirement plan contributions with pretax dollars. For 2021, participants may contribute up to $19,500 ($26,000 if age 50 or older). Taxes on contributions and earnings are deferred until participants take distributions. At that point, withdrawals are included in income, and participants pay taxes based on their tax rate at that time.[1]

In contrast, a Roth 401(k) combines certain features of a traditional 401(k) and a Roth individual retirement account (IRA). As with a Roth IRA, contributions to a Roth 401(k) are made with after-tax dollars. Qualified distributions of contributions—as well as any earnings—from a Roth 401(k) account are income tax free. To qualify for tax-free treatment, a Roth 401(k) distribution must be made after a five-tax-year period beginning with the first tax year for which the participant made a designated Roth contribution under the same plan. Additionally, the participant must have reached age 59½ or the distribution must be made after the participant's death or because of disability. Unlike Roth IRAs, Roth 401(k)s do not allow a qualified distribution for a first-time home purchase.

The maximum annual contribution to a Roth IRA for 2021 is $6,000 ($7,000 if age 50 or older), and eligibility for Roth IRA contributions is phased out as income rises. No such income limits apply to a designated Roth 401(k) account—a feature that might appeal to highly compensated employees. Moreover, plans may allow eligible participants to make designated Roth contributions up to the limits set for traditional 401(k) plans. These limits will apply to pretax and after-tax Roth contributions combined. Employers may make matching contributions on designated Roth contributions, but they must allocate any matching contributions to a pretax account.

A plan may not consist solely of designated Roth accounts—if offering a Roth 401(k) option, the sponsor must also offer a traditional 401(k) plan. Participants may then be allowed to designate some or all of their elective deferrals as Roth 401(k) contributions.

## Implementing a Roth 401(k)

When considering a Roth 401(k) option, sponsors should be aware of the need to comply with additional administrative requirements. To implement a Roth 401(k), the sponsor must adopt an appropriate plan amendment by the end of the plan year for which the amendment is effective. Participants must receive amended plan notifications, including an updated summary plan description and election forms. Educational materials may need to be updated as well.

Plans must keep separate accounts for each participant's Roth 401(k) and traditional 401(k) accounts, and employers will need to change their payroll systems to accommodate Roth contributions. If recordkeeping is outsourced, service providers will need to properly account for Roth 401(k) contributions and any earnings.

## In-plan rollovers

Sponsors may also want to amend their plans to allow participants to make "in-plan Roth rollovers" from their traditional 401(k) accounts to their Roth 401(k)s. Participants who choose to make in-plan Roth rollovers will be subject to income tax

[1] Penalty-free "coronavirus-related" distributions (CRDs) were available in 2020 under the CARES Act.

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on any previously untaxed amounts that are rolled over. However, the 20% withholding requirement that generally applies to eligible rollover distributions does not apply to direct in-plan rollovers. Also, in-plan Roth rollovers are generally not subject to the 10% additional tax on early distributions.

Plans may choose to allow in-plan Roth rollovers even where the amounts are not otherwise distributable under the plan's terms. However, once the rollover is completed, any distribution restrictions that applied before the rollover will again apply to both the rolled over amount and any earnings thereon.

## Nondiscrimination testing

Plans may not discriminate in favor of highly compensated employees when offering a Roth 401(k). Additionally, designated Roth 401(k) contributions are treated as elective contributions for purposes of the actual deferral percentage test.

**The foregoing is a broad overview of the relevant rules. If you are considering adding a designated Roth contribution option to your plan, consult your financial, tax or legal professional.**

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