Outlook for 2006

RETIREMENT PLANN

From Structure to Results: Why We Have to Be Where We Are, Where We Need to Go Now

More employers are including a defined contribution plan in their benefits package every year. According to the Department of Labor's 2004 "National Compensation Survey" 53 percent of all private industry workers, and 62 percent of all those working full time, had access to an employer provided defined contribution plan. This is up from 51 percent and 60 percent respectively in 2003. Also, governments increasingly are offering a defined contribution option. For example, Alaska recently decided to offer its employees a defined contribution program modeled after the Federal Thrift Plan and more governments at all levels are offering 457 plans.

During the past 25 years, America's employers have built the greatest engine for individual retirement wealth accumulation ever developed. From 1982 through 2004 the amount amassed in employer-provided defined contribution plans, and the primarily rollover-funded IRA system, grew from less than $300 billion to approximately $6 trillion. This amount is net of the billions of dollars in benefits being paid out to the increasing number of Americans who are retiring with defined contribution or defined contribution funded IRA balances. Further, I project that with no further legislative change, except permanence for the pension provisions of the 2001 Tax Act (EGTRRA), that this defined contribution plan/IRA accumulation will reach $15 trillion in 2013.

Our defined contribution plan future will be continued evolution driven by a new focus on results, empowered paternalism, automatic solutions and technology-based innovative solutions.

During this 25-year period, the most constant aspect of the employer-defined contribution system has been its continuing evolution. In order to make 401(k) and other defined contribution plans broadly available, an infrastructure had to been built to collect employer and employee contributions, manage the assets and communicate with and educate employees. For example, in the typical 401(k) of the early 1980s, employee contributions were deposited and invested on a quarterly basis. Today the DOL is pushing for a system where employee contributions are deposited in the plan simultaneous with payroll withholding. And, who can complain about a system in which deposits into a plan are virtually instantaneously invested?

Fortunately, there were two pivotal—and favorable—developments that occurred simultaneously. The first was the explosive growth in the power of technology. Without cost effective, powerful technology, a large company would have had to hire a Sears Tower full of clerks to manually maintain and manage the data and processes necessary to support today's defined contribution program. Not only would this be costly and inefficient, but it would not have provided the level of accuracy and timeliness expected by today's participants. For defined-contribution plan recordkeeping, perfect is just good enough. Without the advances in technology, plans would be rigid and user-unfriendly, and even if a plan were offered, participants would be less likely to participate.

The second favorable development was the bull stock market. During the 1980s and 1990s everyone wanted to invest in stocks. For the average worker that meant participation in a 401(k). Asset allocation seemed easy because stock market growth made everyone a successful investor. Plans flourished and account balances grew even as sponsors invested most of their time experimenting with plan design and choosing their plan providers and investment options. Service providers were permitted to spend most of their time and resources on developing 401(k) products and building data management platforms using technology's rapidly increasing functionality.

The development and implementation of an infrastructure capable of managing the accurate, inexpensive and flexible retirement savings program that is today's defined contribution system is one of America's greatest achievements during the last 20 years. Looking forward, we must make sure that the infrastructure we have built and the processes we have put in place deliver results. It is the results, after all, that are the ultimate goal. Some said, "If we build it, they will come." But have they? Yes, most have. Approximately 75 percent of those eligible to participate in 401(k) plans do so. That's a good number, but what about the other 25 percent, and are the 75 percent saving enough? Are they properly invested?

During the last 25 years, a strong foundation was built for the defined contribution system. It's time to capitalize fully

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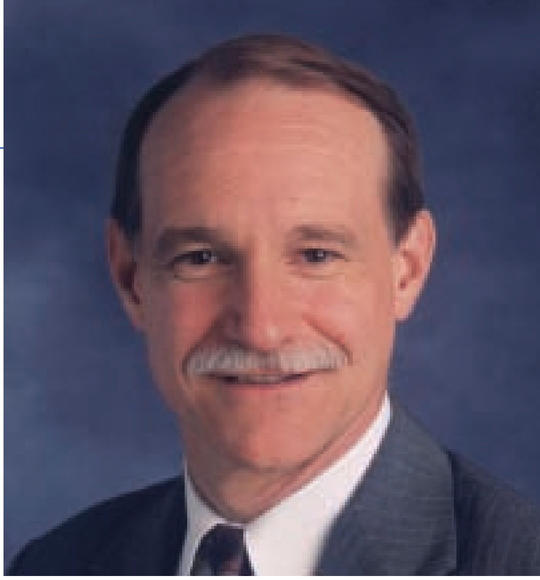

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on its potential and help deliver a secure financial future to every American worker. Our defined contribution plan future will be continued evolution driven by a new focus on results, empowered paternalism, automatic solutions and technology-based innovative solutions.

From Process To Results

In 1999, the Profit Sharing/401(k) Council of America (PSCA) began to focus on the importance of measurement and results. To promote this policy, applications for the 2000 Signature Awards (PSCA's contest to recognize outstanding achievement in plan communications) included measuring results. Today's winners must show not only attractive, innovation communications, but resulting changes in participant behavior.

It is time to go further, and employers have taken the first steps along this new path. Employers not only measure results for their communications programs, but they are starting to establish goals and implement ways to measure the progress of their participants individually and their defined contribution plans as a whole. They are identifying participants who are succeeding and those who are not. They are starting to reach out with the personalized communications and solutions for those who are falling short. They are exploring defined contribution plan approaches designed not just to provide opportunity but to deliver measurable results.

Empowered Paternalism

From its foundation in 1904 until the early 1980s, the defined contribution system was nearly as paternalistic as the traditional pension system. Most plans were completely employer funded and the sponsors invested the plan assets, even in plans where employees could save a portion of their wages. The introduction of the 401(k) changed this. Employers decided that to obtain voluntary employee participation in an employer-sponsored plan, a retail-like structure had to be built around employee choice. Considering the times, this was probably the correct decision. We were in the midst of a major restructuring of American business, and millions in their 40s and 50s had lost their jobs. Trust in the workplace was at low ebb. Also, as the bull market made investing seem easy, employees speaking out about their 401(k) wanted more choice, not less. Today, at only 4 percent of companies with 401(k) plans does the company make the investment decision for their employees.

However, beginning with three straight losing years of equity losses in 2000, the perception of what is best for both the employee and company has been changing. Where many employees had wanted more control over their plan assets, they began to welcome employer-provided investment management. Prior to 2000 most plan sponsors did not offer investment advice partially because participants did not want it. Participants today are looking to their employer for help, and more than 50 percent of employers now offer investment advice. Within a few years advice will be a standard 401(k) plan feature.

In the future, retirees will be able to maintain their lump sum but gradually annuitize some or all of their deferred accumulation considering their individual risk, investment and estate preferences.

Companies are also recognizing that they need to be more proactive in helping their plan participants reach their retirement savings goals. The company's purpose for offering a defined contribution plan is to attract, retain and motivate high-quality workers. If employees are not participating or are making unwise plan-related decisions, the company does not benefit from the time and resources it is investing to operate and fund its defined contribution program.

It is mutually beneficial for companies and employees that employers do more than just offer the opportunity to save for retirement. Sponsors will increasingly take a greater role in the management of their defined contribution plans. Employees still will have choices. It is still about empowerment. But there will also be paternalism. The future will be based on empowered paternalism.

Automatic Solutions

Companies are starting to automatically enroll eligible employees in their 401(k) plans. For those new to the topic,

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Now add to the list of tasks identified above the requirements inherent in incorporating the administration of HRAs and HSAs into your line of products. Three-plus years of Treasury Rulings, along with multiple developing technologies, have spawned both an opportunity (i.e., for increased revenues) and an obligation (i.e., a need to provide a higher level of service). Not only must the claims process be integrated to allocate a flex claim across multiple accounts (each with unique balances, plan parameters and claims rules) and multiple plan years, but an increase in the number of employer funded arrangements (e.g., HRAs) will significantly impact accounting and reporting requirements.

New technologies supporting flex debit card processes allow for increased auto-adjudication and higher participant satisfaction, but for every benefit of the card perceived by plan participants, there is a commensurate administrative responsibility foisted upon the administrator. The need to synchronize account balances between the in-house manual system and the electronic debit card system is an ominous task that some flex software vendors have publicly claimed to be unrealistic, if not impossible. Now factor in the technological developments in self-service, web-based conveniences and it should quickly become apparent that traditional spreadsheet applications and entry-level flex systems leave much to be desired. For the larger TPA relying on the home-grown system, the time and resource commitment necessary to keep pace with so many changes is like trying to hit a rapidly moving target. As such, it can seriously impact your bottom line!

In 2006 and beyond, in order to take advantage of these many opportunities, you will need a more sophisticated flex administration system, one that is dynamic. It's clearly time to turn to the software experts who do what they do best.

Our P+W Software solution, POWERPLUS, has been the most reliable, most powerful and most dynamic flex solution for nearly 20 years.

Our clients were among the first in the country to offer employers HRAs, HSAs and TRAs, as the inherent flexibility of POWERPLUS made it easy for us to introduce this functionality into our base system, not via an optional, extra-cost, add-on module.

Our clients were the first to offer a choice of debit card vendors, since we integrate our system to all of the three leading flex debit card companies. We pioneered the concept of the debit card interface, and today, over 300,000 flex participants use debit cards synchronized to the POWERPLUS system.

POWERPLUS users around the country are already processing claims during Grace Periods. Our extensive background in Flexible Benefits Administration and software development has allowed us to respond quickly and properly to the recent Treasury Ruling on the 2 ? month extension.

As I've said many times, each commercial flex system is a good system, for someone. A little due diligence and astute evaluation on your part will help you choose the option that will work best for you. Start taking advantage of the opportunities today, so that in 2006 and beyond, you will still be one of the industry's leaders!

David Wray

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automatic enrollment is when the employer enrolls the employee in its 401(k) plan unless the employee elects not to participate.

The most compelling reason for automatic enrollment is that it can increase plan participation. It is realistic to expect that over time, the use of automatic enrollment will result in a plan participation rate of 95 percent or better. This higher participation rate is most noticeable among younger, lower-paid workers who traditionally are more hesitant to become involved in retirement savings programs.

Employers are also increasingly using plan features in which the employees' investments will be automatically invested and rebalanced. Some companies have even started automatically increasing the amount of an employees' wages contributed to the plan. Beginning this year, some companies have begun automatically rolling over termination balances between $1,000 and $5,000 into an employer-selected IRA. The common characteristic of these programs is that an employer-selected solution happens unless the participant opts out.

In addition, government policymakers are moving to encourage these automatic solutions. Legislation currently being considered by Congress includes provisions that encourage the adoption of automatic enrollment by removing perceived barriers under ERISA and the provision of a safe harbor for plans that include an automatic annual increase in the participant's savings rate.

Technology-Based Solutions

The employer-provided defined-contribution system will continue to benefit from new and better solutions using our increasingly powerful technological tools. For example, few retiring defined-contribution participants annuitize their lump sums. Faced with a one-point-in-time, all-or-nothing irrevocable choice, they overwhelming choose to retain their assets in lump sum form. In the future, however, retirees will be able to maintain their lump sum but gradually annuitize some or all of their deferred accumulation considering their individual risk, investment and estate preferences. When they decide to purchase an annuity they will be able to go online and obtain institutional prices from the highest bidder.

The employer provided defined contribution system continues to evolve. The only certainty is that the amounts generated by this system are going to be enormous, and enormously beneficial for American workers.

For more information on companies, see our Resource Guide page 51.