

# Target Date Funds

## So Many Choices...So Little Information

by Patrick M. Fay

I recently had the opportunity to have lunch with Fred Reish, a Los Angeles attorney who is widely considered to be the foremost expert on ERISA and 401(k) law. One of the topics we discussed was Target Date Funds (TDF) and how they function in a retirement plan.

TDFs (also known as lifecycle or age-based funds) have become a popular tool for retirement plan creation because they allow an investor to link his or her investment portfolio to a specific time horizon (most generally, that individual's retirement date). SilverStone Group has successfully incorporated TDFs into many retirement plans, joining the 25-80% of plans that now utilize this type of fund. Reish believes that number will continue to grow as employees and plan sponsors better understand the benefits that TDFs can offer.

### Discovering fund versatility

During the recent bear market, many articles critiqued TDF management techniques. As with other mutual funds, TDF management styles incorporate a spectrum from conservative to aggressive. It is the responsibility of the plan sponsor and investment advisor to understand the differences and determine which style is most suited to plan demographics.

As an example, a manufacturing company provides both a 401(k) plan and a relatively conservative Defined Benefit (DB) plan. The plan committee and its advisor examine the plan demographics and determine that, because they offer a DB that provides a reliable (and conservative) source of income for retired employees, the organization wants to offer a more aggressive TDF option.

On the other hand, the company could decide that because it is a conservative organization whose workers have little investment knowledge, and because the DB plan already assures employees of income at retirement, its TDF options should be more conservative.

The decision made in each scenario is correct, given the difference in plan objectives. These examples demonstrate that a TDF can be a viable choice for any plan, whether one chooses an aggressive or conservative position.

### Education matters

Fred Reish suggests that employers who offer retirement plans should also offer investment education. Reish's recommendation is for an employer to transition all employee retirement accounts into an appropriate TDF. He further counsels that employers should precede this action with proper notification, educational opportunities regarding TDFs and their benefits and plenty of lead time so that those who wish to retain personal control of their funds can opt out of the automatic selection. Employees whose accounts automatically default to a TDF would be enrolled at an age-appropriate fund level. The federal government sanctions a TDF default investment policy and has determined that employers who choose this method are plan fiduciaries.

It's important to remember that a 401(k) plan is a retirement savings plan. An important goal of any plan should be to help employees accumulate enough assets for retirement. The challenge employees face is how to make proper investment decisions—giving people investment information and expecting them to muddle through without guidance has not been a successful strategy in the past. Utilizing TDFs in the retirement plan provides an opportunity for employers and plan sponsors to advise employees about investment options and educate them on the importance of building a solid retirement fund.

While a TDF may not be appropriate in all instances, it is a measure that can be considered at your annual investment committee meeting. Remember, the TDF you choose is not as important as the development of a process that encourages an organization's employees to plan for a successful retirement.

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