

City of Los Angeles Deferred Compensation Plan

Defined Contribution Trends and Regulatory, Judicial & Legislative Review

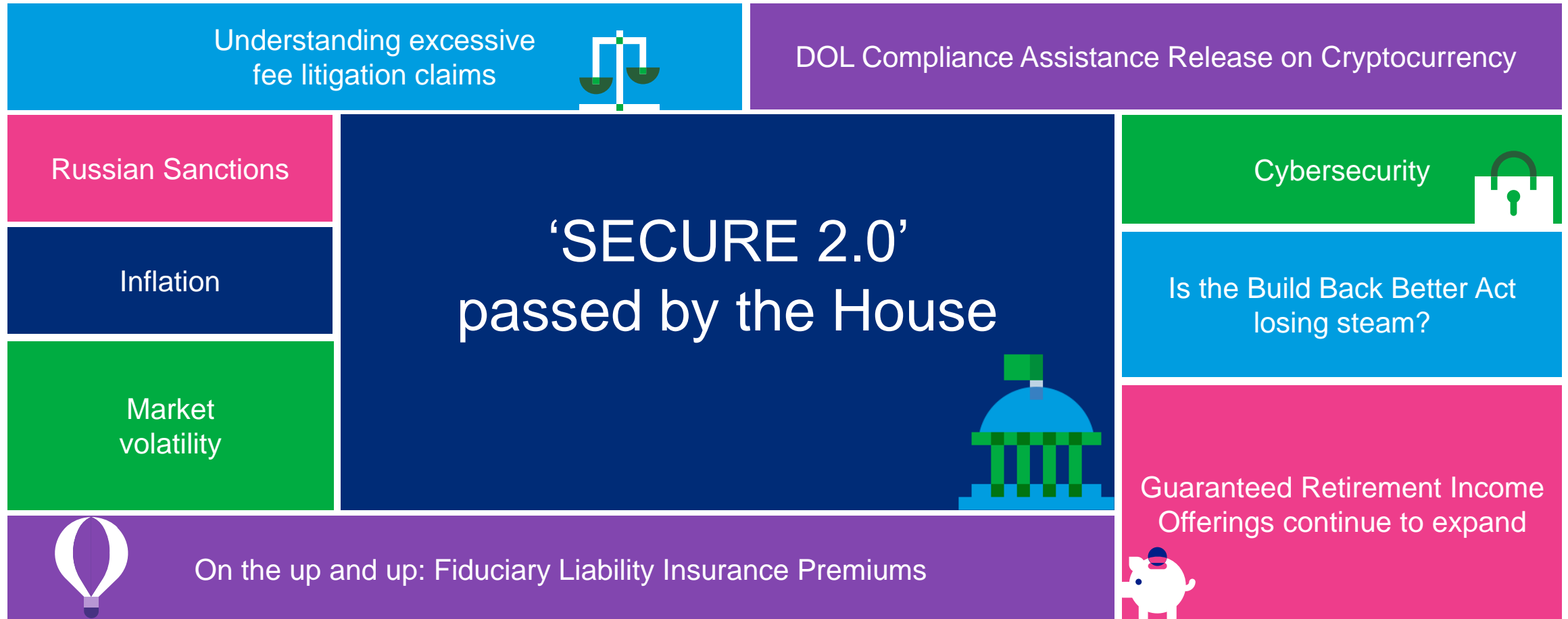
July 2022



Agenda

- DC landscape at a glance
- Regulatory, judicial & legislative updates
- Trending topics
- City of LA comparative trends

DC landscape at a glance



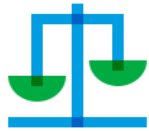
Regulatory, Judicial & Legislative Updates

Judicial update

Litigation and enforcement

Cases by the numbers for Q1 2022¹

Cases closed



8 settlements
\$47.6 Million



8 dismissals
Includes partial and full dismissals

Cases by key theme



2 stock/ESOP



2 proprietary investments



23 fees and investments



**4 target risk/
target date funds**



3 plan administration



**1 403(b) plan/
not-for-profit**

¹ Information sourced through Law360, Pensions & Investments, NAPA and PlanSponsor as of April 15, 2022. Cases listed represent some recent litigation and are not intended to be a complete representation.

Judicial update

Litigation and enforcement

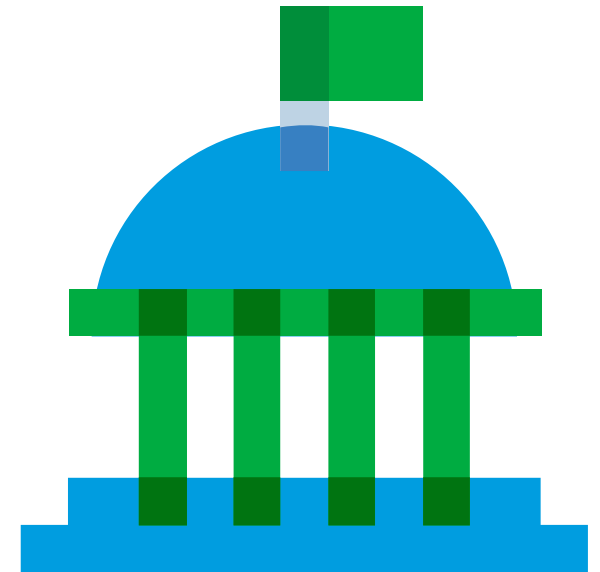
Recent areas of focus

- ⓘ Reasonableness of recordkeeping fees and allocation of revenue sharing
- ⓘ Reasonableness of investment management fees (mutual fund share classes vs. collective trusts vs. separate accounts)
- ⓘ Offering active vs. passive funds
- ⓘ Appropriateness and performance of funds offered, including target risk and target date funds
- ⓘ Offering proprietary products
- ⓘ Plan administration – fraudulent hardship withdrawals, failing to remit contributions

List represents some recent trends and is not meant to be a complete representation.

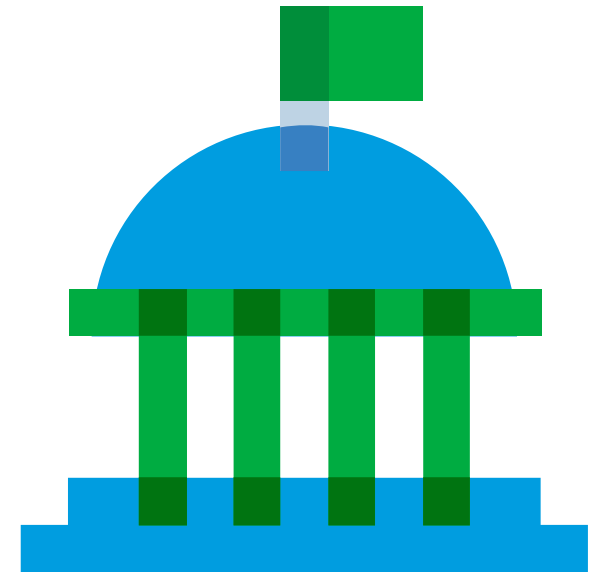
Broad 'SECURE 2.0' bill sails through House

- **Array of bipartisan reforms in the Securing a Strong Retirement Act (HR 2954) including:**
 - Student loan repayment may earn matching contributions
 - Voluntary self-corrections of inadvertent errors
 - Simplified reporting, disclosure requirements
 - Support for lifetime income options
 - 403(b) plan enhancements
 - Cash-out minimum increased to \$7,000
 - Increase age for RMDs to 75
 - Higher catch-up contributions for older workers
 - Expanded coverage for long-term part-time workers
 - Retirement savings “lost and found” database
 - Optional recoupment of overpayments



Broad 'SECURE 2.0' bill sails through House, cont'd.

- **Securing a Strong Retirement Act would direct more savings to Roth accounts**
 - Mandated Roth treatment for catch-up contributions
 - Matching contributions permitted on Roth basis
- **Issues in play as action moves to the Senate**
 - Mandated auto-enrollment/escalation for new plans
 - Missing participants
 - E-delivery/annual paper benefit statement
 - Spousal consent for DC plan distributions
 - Emergency savings
- **Senate committees drafting counterpart legislation**
 - Bills expected late Spring/Summer
 - Final measure could pass Congress later this year



'Secure 2.0' – Breaking down the provisions

Participant focused

- **Expanded coverage of part-time workers**
- **Student loan matching payments**
- Mandated automatic enrollment and escalation for new plans
- Changes to required minimum distributions
- Withdrawal changes
- Increase catch-up contribution limits

Plan sponsor focused

- Expanded self-correction program & reliance on self-certifications
- Retirement savings lost and found
- **Amendments to qualified longevity annuity contracts (QLACs)**
- **403(b) plans can join PEPs; support for collective trusts**
- Increased credits for small employers
- Simplified reporting & disclosure requirements

Revenue-raising

- Mandated Roth treatment for catch-up contributions
- **Matching contributions permitted on Roth basis**

Bolded provisions indicate areas Mercer believes will have especially notable impact

Recent DOL guidance

Compliance Assistance Release No. 2022-01

- **DOL has “serious concerns” about fiduciaries “exposing” participants to crypto investments**
 - As direct investment option
 - Through brokerage windows
- **DOL intends to investigate plans that allow crypto investments to determine whether fiduciaries complied with ERISA duties of prudence and loyalty**
- **Guidance directed at 401(k) plan fiduciaries, but all DC-plan fiduciaries should take note**

Mercer GRIST: [DOL sends strong warning to 401\(k\) plan fiduciaries about cryptocurrency \(03/16/22\)](#)

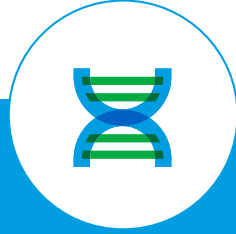
Trending topics

Top considerations for DC plans in 2022



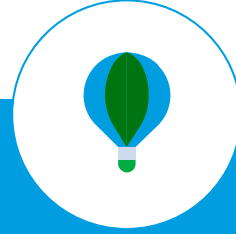
DATA IS KING: Are you crunching the numbers?

- Refine retirement programs with participant data and behavioral trends
- Engagement and participant experience with your recordkeeper
- Data and cybersecurity



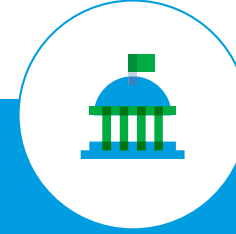
INVESTMENT PRODUCT EVOLUTION: Are you keeping up with new investment products?

- ESG
- Retirement income
- Inflation protection
- Managed accounts and personalization
- Private investments



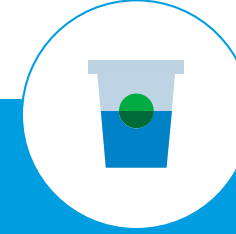
THE BIG KEEP GETTING BIGGER: Is growth a problem?

- Recordkeeper & investment manager consolidation and implications
- Capacity constraints and custom multi-manager funds



THE MERRY-GO-ROUND OF WASHINGTON DC: How will legislation & regulation impact your plan in 2022?

- Position for design opportunities



CUPS ARE OVERFLOWING: How are you managing your fiduciary responsibilities?

- Fiduciary insurance burdens

Retirement income

In focus: In-plan annuities

The retirement income marketplace comprises a broad range of topics, products, and offerings

- Solutions: providing both guaranteed and non-guaranteed income
- Tools and resources: retirement planning and projection tools and targeted communication strategies
- Advice features: including managed accounts and financial coaching

Evolving retirement plan landscape has led to a shift in focus toward guaranteed income solutions in DC plans

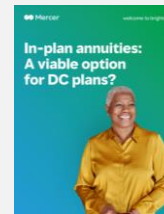
- Shifting regulatory environment including passage of SECURE
- DC plans becoming the core retirement source for more private sector workers each year
- More retirees entering retirement now than ever before with 10,000 baby boomers turning 65 per day*
- Retirees face challenges protecting against risks like longevity and inflation

Standalone in-plan annuities

- New service providers and offerings coming to the DC market will provide retirees with easier access to annuities in DC plans

→ **Path A:**
Recordkeeper offerings

→ **Path B:**
Annuity provider offerings



[In-plan annuities: A viable option for DC plans?](#)

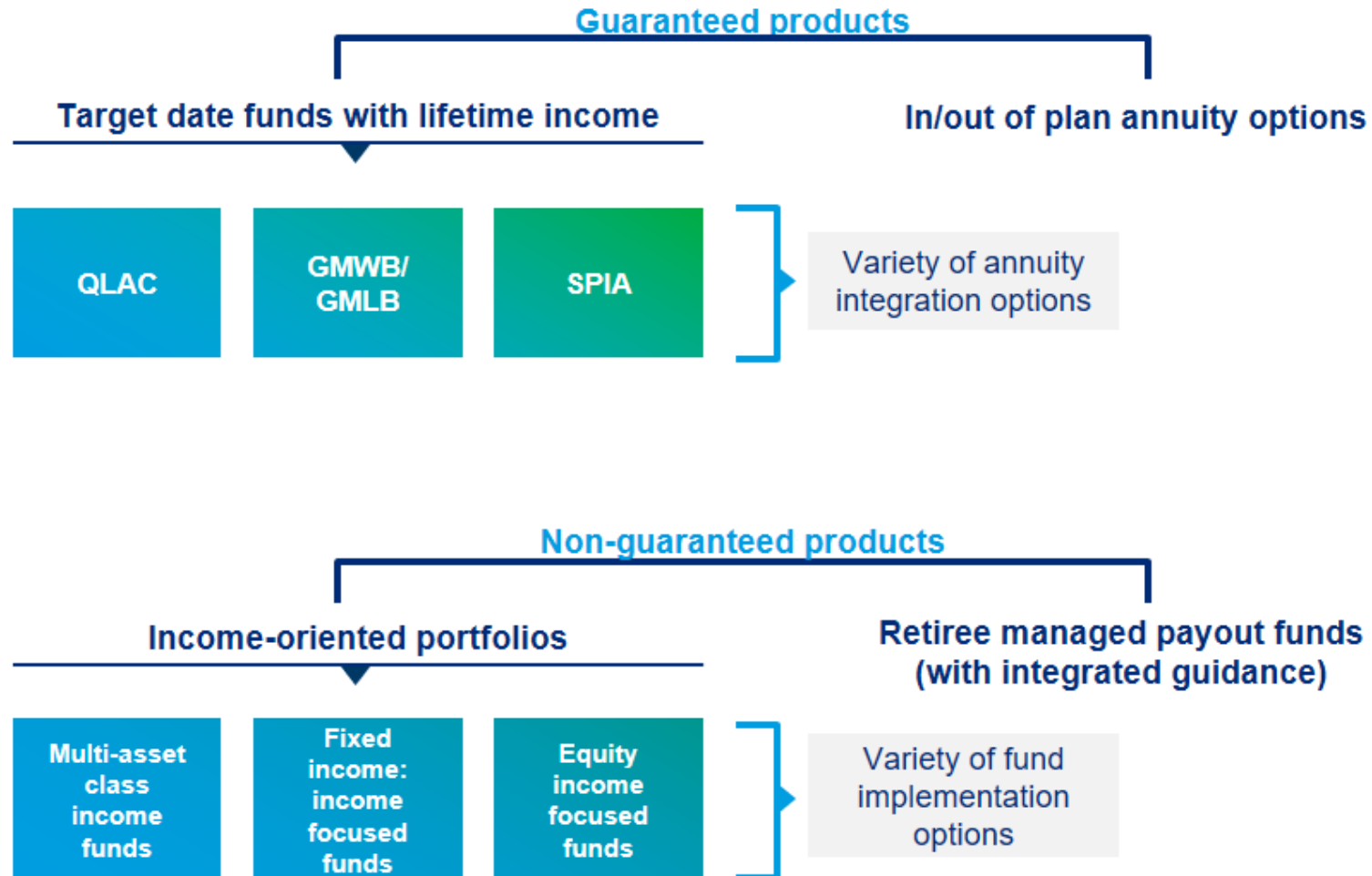
Steps to meet fiduciary responsibilities in selecting and monitoring in-plan annuity offerings:

1. **Understand:** the offering and annuity providers available and determine whether they meet the objectives of the plan
2. **Evaluate:** annuity provider(s) based on fiduciary standards laid out in the SECURE Act
3. **Select:** annuity provider(s) and offering to be made available to plan participants
4. **Monitor:** on an ongoing basis and perform a formal review annually

*Pew Research Center, February 25, 2019

Retirement income investment solutions

Guaranteed and non-guaranteed options



Fiduciary best practices

Best practices



- Form a Retirement Plan Committee
- Know your role and responsibilities
- Hire experts
- Understand service provider contracts
- Ensure reasonableness of Plan fees
- Use fiduciary protection tools
- Comply with plan operational provisions
- Follow procedural prudence
- Document decisions and actions

Fiduciary liability insurance

Expectations and key considerations

- In 2021 we saw more insurers pulling back on Fiduciary insurance. Expectations set for renewals may change at the last minute:
 - The average premium increased 40% in the fourth quarter of 2020.
 - Insurers are focusing on class action/excessive fee retentions¹. For plans with assets over \$250 million, insurers will likely seek retentions more than \$1 million...in many cases \$5 million or \$25 million.
 - Primary insurers are cutting capacity, in many cases to \$5 million.
 - Insurers are imposing higher retentions¹, sub-limits, and increased pricing, regardless of the policyholder's due diligence in this area; expect more underwriting questions or questionnaires.
 - Insurers will likely ask about recordkeeper fees for benchmarking purposes and will question whether an RFP has been carried out.
 - Larger defined contribution plans will likely see little insurer competition from new markets. It is important to highlight controls, fee benchmarking, and process to attract new insurers.

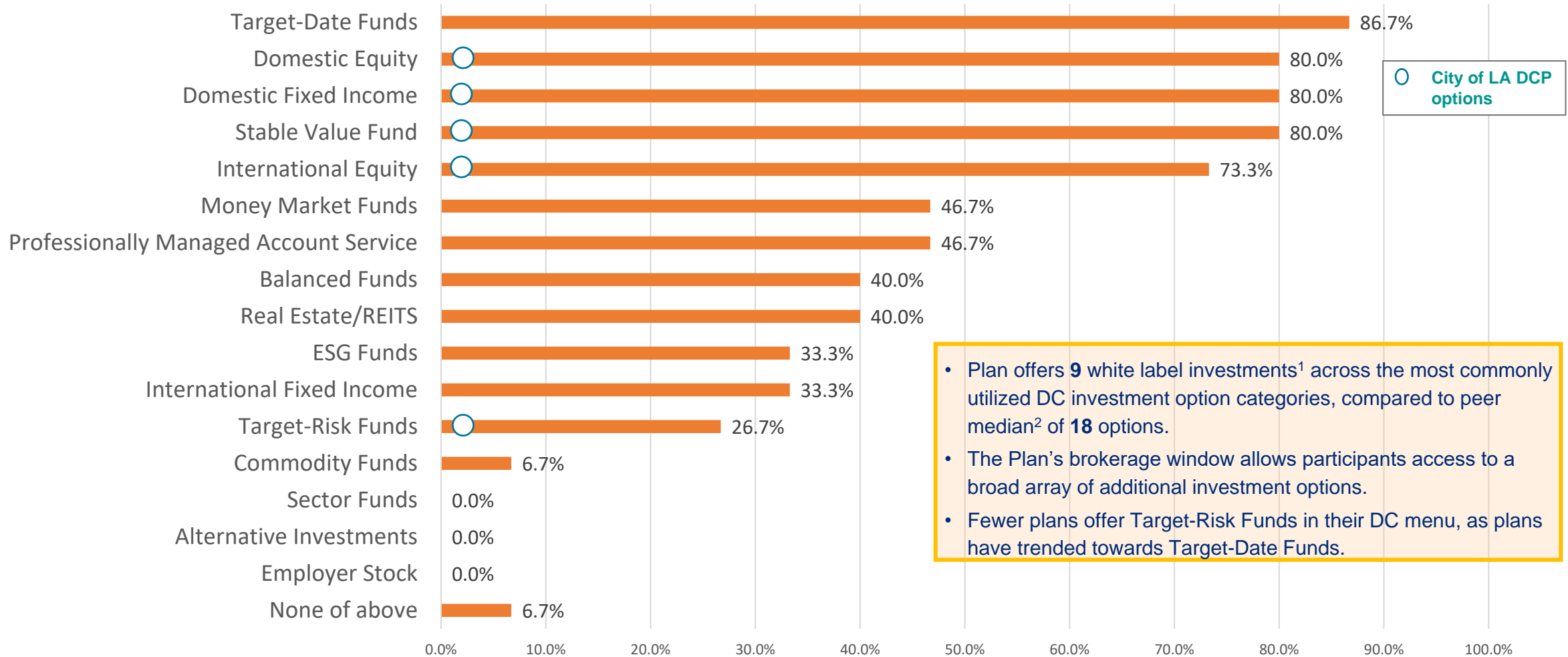
Considerations

- The keys to a successful renewal are early preparation and a crisp well laid out explanation of the risk controls in place.
- Governance model can have implications on availability of liability insurance. For example, a Plan engaged in a 3(38) OCIO relationship may have more optionality and potentially receive more favorable terms from insurers as compared to a Plan receiving 3(21) advice.
- There is no hard and fast rule in regards to the amount of coverage a Plan should carry so it is important to go through the exercise of receiving custom pricing based on your plan and specifics.

City of LA Comparative Trends

Market trends and comparative review

Investment option prevalence



- Plan offers **9** white label investments¹ across the most commonly utilized DC investment option categories, compared to peer median² of **18** options.
- The Plan's brokerage window allows participants access to a broad array of additional investment options.
- Fewer plans offer Target-Risk Funds in their DC menu, as plans have trended towards Target-Date Funds.

Source: PlanSponsor Defined Contribution Survey, 2022 – 457 Plans; Mega (>\$1B); 17 respondents

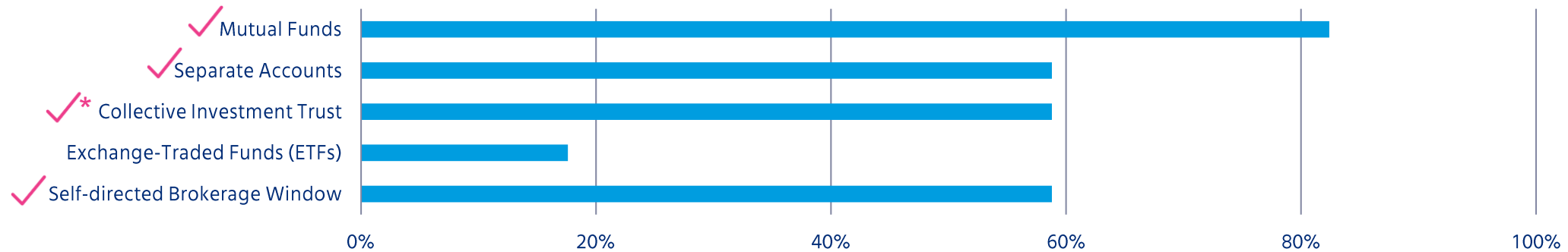
¹ Counting 5 target risk funds as 1 option; including FDIC-Insured Savings Account and brokerage window. As plans get larger the number of options reduces.

² Peer median is given for mega plans (>\$1 billion) in the 457 plan category based on PLANSPONSOR 2022 report.

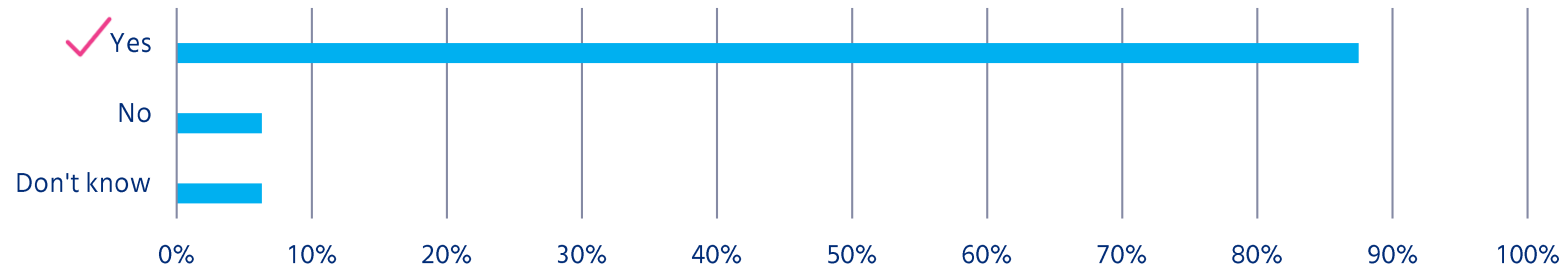
PlanSponsor Survey – 457 Plans >\$1 Billion

Comparative Analysis

Investment Vehicle Prevalence



Passive Investments Offered



Note: It is likely these are standalone/discrete options (i.e. not blended into the core funds)

Source: PlanSponsor Defined Contribution Survey, 2022 – 457 Plans; Mega (>\$1B); 17 respondents

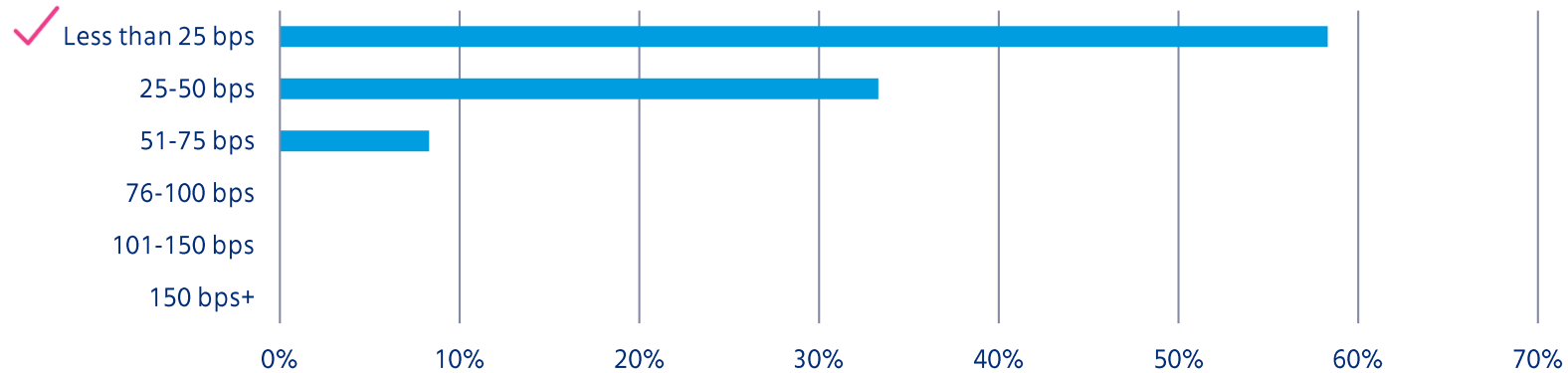
✓ Denotes a feature in the City of LA DCP

* Pending implementation. Contract negotiation is currently underway with the investment managers selected.

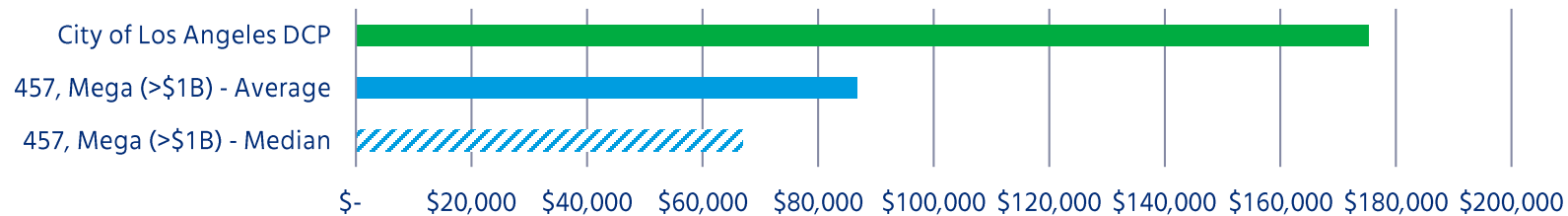
PlanSponsor Survey – 457 Plans >\$1 Billion

Comparative Analysis

Average Asset-Weighted Expense Ratio



Average Account Balance



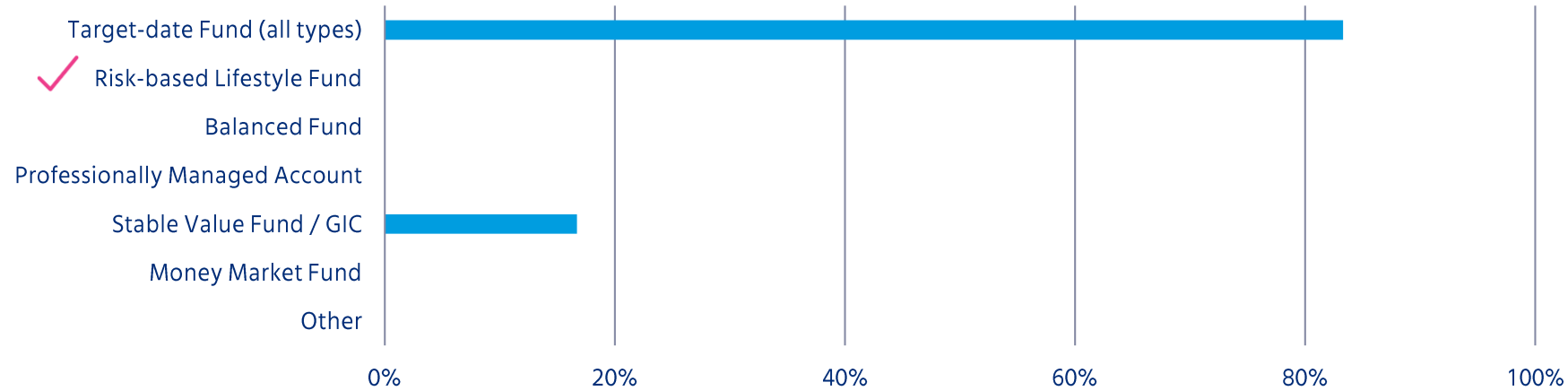
Source: PlanSponsor Defined Contribution Survey, 2022 – 457 Plans; Mega (>\$1B); 17 respondents and Voya's 1Q22 Report

✓ Denotes a feature in the City of LA DCP

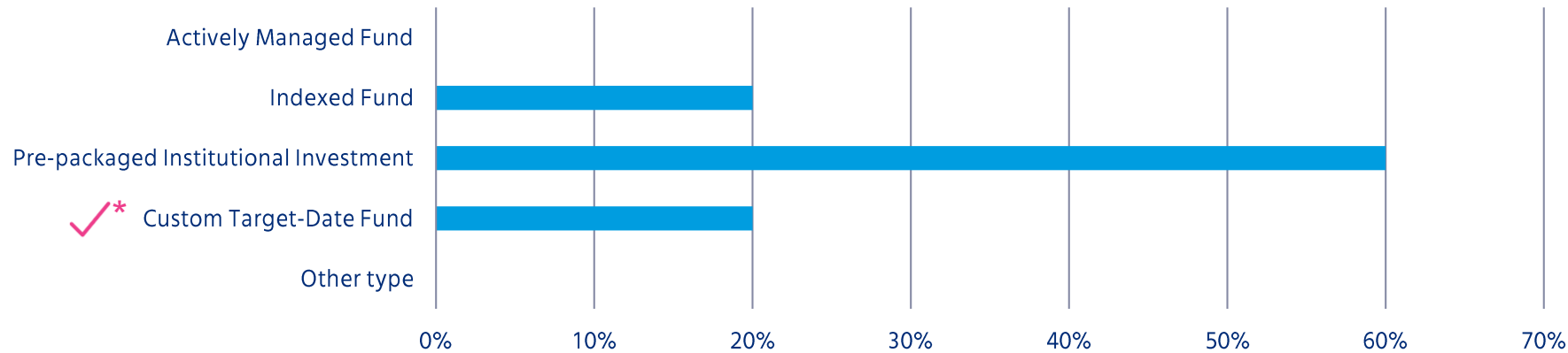
PlanSponsor Survey – 457 Plans >\$1 Billion

Comparative Analysis

Prevalence of default investment type



Type of target-date fund used as a default investment



Source: PlanSponsor Defined Contribution Survey, 2022 – 457 Plans; Mega (>\$1B); 17 respondents

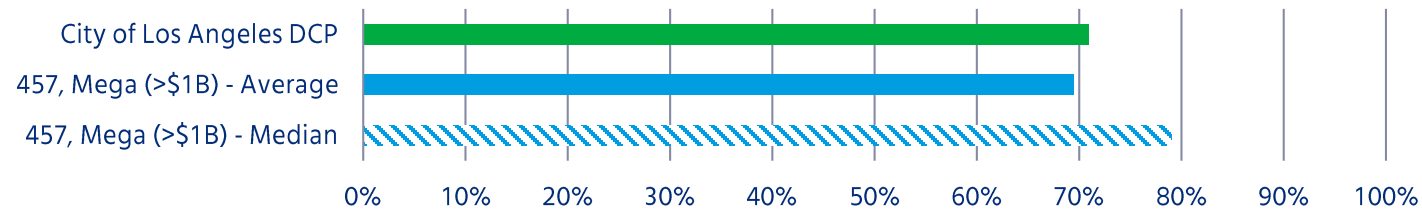
✓ Denotes a feature in the City of LA DCP

* The City utilizes custom Target Risk Funds

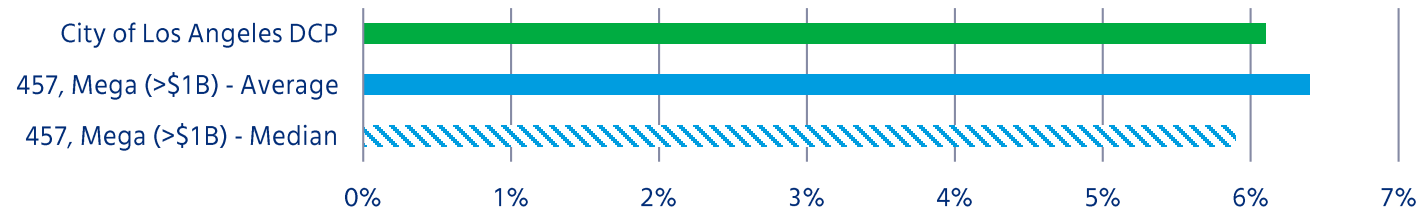
PlanSponsor Survey – 457 Plans >\$1 Billion

Comparative Analysis

Participation Comparison



Employee Deferral Comparison

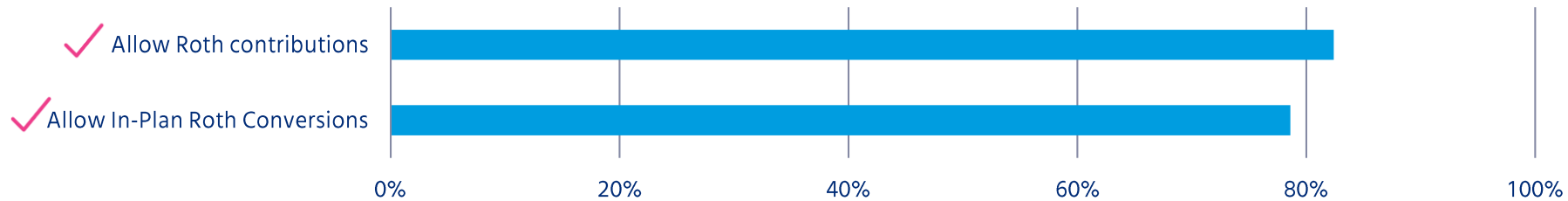


Source: PlanSponsor Defined Contribution Survey, 2022 – 457 Plans; Mega (>\$1B); 17 respondents
DCP's Participation Rate and Employee Deferral Rate provided by Voya as of 3/31/22

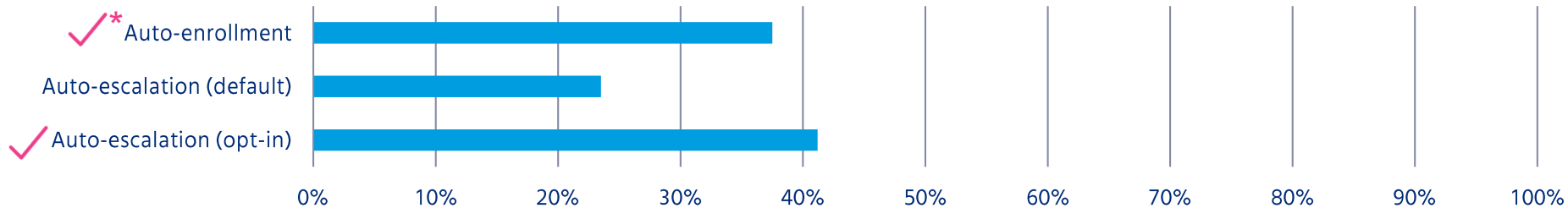
PlanSponsor Survey – 457 Plans >\$1 Billion

Comparative Analysis

Roth Features



Prevalence of Auto Features



Source: PlanSponsor Defined Contribution Survey, 2022 – 457 Plans; Mega (>\$1B); 17 respondents

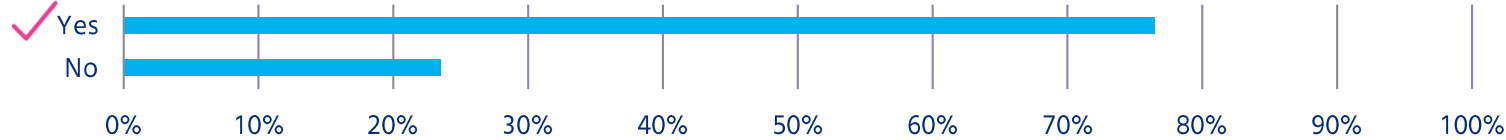
✓ Denotes a feature in the City of LA DCP

* Pending implementation. Currently just the Police Union has the auto-enrollment feature.

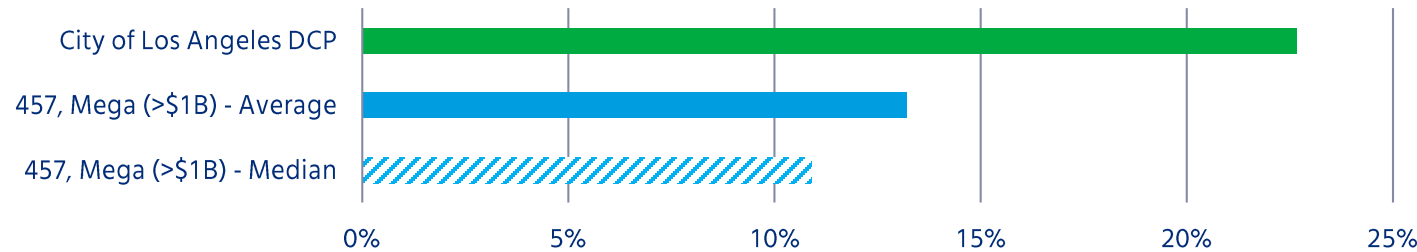
PlanSponsor Survey – 457 Plans >\$1 Billion

Comparative Analysis

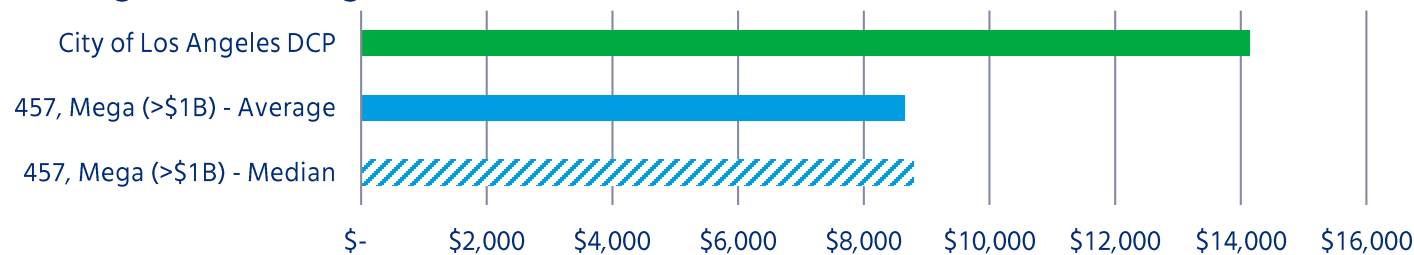
Loan Provision



Percentage of participants with outstanding loans



Average Outstanding loan balance



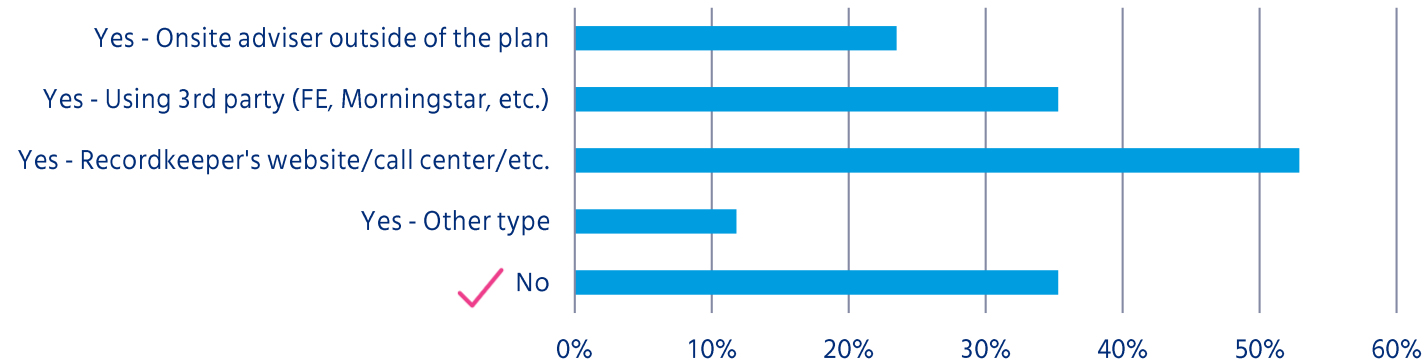
Source: PlanSponsor Defined Contribution Survey, 2022 – 457 Plans; Mega (>\$1B); 17 respondents and Voya's 1Q22 Report

✓ Denotes a feature in the City of LA DCP

PlanSponsor Survey – 457 Plans >\$1 Billion

Comparative Analysis

Financial/Investment Advice Offered



Source: PlanSponsor Defined Contribution Survey, 2022 – 457 Plans; Mega (>\$1B); 17 respondents and Voya's 1Q22 Report

✓ Denotes a feature in the City of LA DCP

Appendix

Annuity definitions

Deferred annuity

A contract that pays a guaranteed income for the rest of your life, but only starts at some future date.

GMWB

Guaranteed Minimum Withdrawal Benefit, a type of variable annuity also sometimes known as GLWBs – Guaranteed Living Withdrawal Benefits – guarantees an income that lasts for life while at the same time providing liquidity and access to asset allocation. Products that feature a GMWB can also protect your retirement income from market downturns and potentially increase if the markets perform well.

QLAC

Qualified Longevity Annuity Contract is essentially a deferred income annuity where the income is deferred to a later age, 80 or 85, but also subject to certain “qualifying” provisions.

SPIA

Single Premium Immediate Annuity is a contract that pays a guaranteed income for the rest of your life, and starts immediately.

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