Volume 31
Number 5
May 2021

Insider

DOL issues cybersecurity tips and best practices

By Gary Chase, Bill Kalten and Ben Lupin

The DOL recently issued three pieces of guidance on cybersecurity best practices for employee benefit plan sponsors, fiduciaries, recordkeepers, participants and beneficiaries: (1) **Tips for Hiring a Service Provider With Strong Cybersecurity Practices**, (2) **Cybersecurity Program Best Practices,** and (3) **Online Security Tips**. This is the first time the DOL has issued comprehensive guidance specific to cybersecurity.

Retirement plan sponsors and fiduciaries should anticipate that their cybersecurity practices will be subject to DOL scrutiny. Significantly, the guidance formally states that "[r]esponsible plan fiduciaries have an obligation to ensure proper mitigation of cybersecurity risks." And at a conference last October, a DOL official previewing the guidance indicated at that time that he expects to see more focus in the department's investigations on the adequacy of various cybersecurity programs, especially for large plans in terms of making sure the providers they hire are observing good cybersecurity practices.

Background

In February 2021, the Government Accountability Office (GAO) released a report requested by Congress on steps the DOL could take to mitigate cybersecurity risks for defined contribution retirement plans. The report also recommended that the DOL 1) formally state that a plan fiduciary is responsible for mitigating cybersecurity risks, and 2) establish minimum expectations for addressing those risks.

In response, the DOL released three pieces of non-binding guidance, primarily directed toward retirement plans, which the DOL explains are prime targets for cybersecurity criminals due in part to the large amount of assets they hold (estimated to be approximately $3.8 trillion in 2018). Although potentially applicable to ERISA-covered health and welfare plans, many of the best practices overlap with the security standards for securing protected health information under the Health Information Portability and Accountability Act (HIPAA). Health plan sponsors may want to review both the DOL's cybersecurity guidance and HIPAA when evaluating a service provider's cybersecurity capabilities.

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Tips for Hiring a Service Provider

The DOL's Tips for Hiring a Service Provider are intended to help plan sponsors and fiduciaries meet their responsibilities under ERISA when selecting service providers that will handle plan records or participant data.

The tips include asking a vendor about the following during the selection process:

- The vendor's information security standards and other cybersecurity-related practices and policies (including whether an outside auditor reviews and validates cybersecurity), and how they compare with industry standards

- How the vendor validates those practices, the level of security standards that have been met and implemented, and whether the contract will provide for the right to review audit results demonstrating compliance with the security standards
- The vendor's past experiences with cybersecurity incidents and security breaches
- Whether the vendor has an insurance policy covering cybersecurity and identity theft (for internal and/or external threats)

These questions may also be helpful when reviewing the cybersecurity practices of an existing recordkeeper or vendor.

The DOL also suggests evaluating the service provider's track record in the industry, including public information regarding information security incidents, other litigation and legal proceedings related to the vendor's services.

In addition, the tips include cybersecurity-related provisions that may be helpful to include or avoid in a vendor contract.

Cybersecurity Program Best Practices

The Cybersecurity Program Best Practices guidance provides detailed recommendations on 12 best practices for recordkeepers and service providers responsible for plan-related IT systems and data. These should also be used by plan fiduciaries when deciding which service providers to hire, and they may be helpful for plans that maintain their own plan administration systems, plan records or data.

The recommendations cover such topics as establishing and documenting a cybersecurity program, conducting risk assessments and audits, providing training, using encryption for sensitive data and responding to cybersecurity incidents.

It is important to note that the DOL also includes a list of items it would "expect to see" in an effective audit program, a signal that the DOL might cover cybersecurity issues in its audits.

Finally, this document is noteworthy for the DOL's statement (without providing any background or explanation) that fiduciaries are responsible for overseeing efforts to mitigate cybersecurity risks. The DOL also signals that cybersecurity could be covered during DOL audits.

Online Security Tips

The final piece of guidance is a list of best practices intended to help plan participants and beneficiaries protect their retirement accounts; however, the Online Security Tips are broad enough that they can apply to a range of online activities. Tips include suggestions for setting up, monitoring and securing online accounts; recommendations for avoiding phishing attacks; and links for reporting identity theft and cybersecurity incidents.

Going forward

Plan sponsors and fiduciaries should review the DOL's tips and best practices to better manage cybersecurity and DOL audit risks and consider using them when:

- Selecting a new recordkeeper or other service provider and during the contracting process, to help evaluate vendor cybersecurity practices
- Evaluating existing vendors and renewing contracts, since fiduciary responsibility includes oversight and monitoring of existing vendors
- Evaluating current IT security programs, for plans that handle IT systems and data internally

Although not required, plans should also consider providing participants and beneficiaries with a copy of the Online Security Tips. Note that the Online Security Tips are not subject to ERISA's distribution requirements, so the notice may be shared through any preferred method (e.g., on the sponsor's intranet, in an employee newsletter or via email).

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***Insider* is a monthly newsletter developed and produced by Willis Towers Watson Research and Innovation Center.**

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IRS announces 2022 HSA, HDHP and EB-HRA dollar limits

By Cindy Brockhausen and Ben Lupin

In **Revenue Procedure 2021-25**, the IRS announced the calendar year 2022 inflation-adjusted dollar limits for health savings accounts (HSAs) and high-deductible health plans (HDHPs), effective for calendar year 2022. Revenue Procedure 2021-25 also includes the maximum annual amount that may be made newly available for excepted benefit health reimbursement arrangements (EB-HRAs), effective for plan years beginning in 2022. These amounts are updated annually to reflect cost-of-living adjustments.

Plan sponsors should consider these limits when planning for the 2022 plan year, as the changes will affect benefit plan administration and communication materials.

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2022 vs. 2021 HSA, HDHP and EB-HRA dollar limits

	2021	2022	Change
HSAs: Maximum annual contribution			
Self-only coverage	**$3,600**	**$3,650**	**+$50**
Family coverage	**$7,200**	**$7,300**	**+$100**
Catch-up contribution for participants age 55 and older by December 31 (this amount is fixed by statute and is not subject to cost-of-living adjustments)	**$1,000**	**$1,000**	**$0**
HDHPs: Minimum annual deductible			
Self-only coverage	**$1,400**	**$1,400**	**$0**
Family coverage	**$2,800**	**$2,800**	**$0**
HDHPs: Maximum annual out-of-pocket amounts (deductibles, copayments and other amounts, but not premiums)			
Self-only coverage	**$7,000**	**$7,050**	**+$50**
Family coverage	**$14,000**	**$14,100**	**+$100**
EB-HRAs			
Maximum annual amount that employers may contribute	**$1,800**	**$1,800**	**$0**

IRS issues guidance on taxation of DC FSAs due to recent changes

By Maureen Gammon and Ben Lupin

In **Notice 2021-26**, the IRS addresses the taxation of dependent care benefits provided through a dependent care flexible spending account (DC FSA) in taxable years ending in 2021 and 2022. The guidance covers (1) the application of either (but not both) the carryover or the extended claims period allowable under the Consolidated Appropriations Act (CAA),[1] and (2) the allowable increase in the maximum contribution limit for the 2021 taxable year under the American Rescue Plan Act (ARPA).[2]

Taxation of carryover or extended claims period

The notice states that individuals who carried over money for dependent care to the following year as part of a DC FSA can avoid tax on that money if they were eligible to avoid tax in the *previous* year. Consequently, DC FSA benefits that would have been excluded from income if used during the preceding taxable year (ending in 2020 or 2021) remain excludable from the employee's gross income. Unused amounts carried over from prior years or available during an extended period for

[1] See "**IRS guidance on FSA flexibility under CAA**," *Insider*, March 2021.

[2] See "**Health and benefit implications of ARPA**," *Insider*, March 2021.

incurring claims will *not* be taken into account when applying the dollar limits to other dependent care benefits available for the taxable years ending in 2021 and 2022.

For a calendar-year plan, for example, this would mean that a $5,000 carryover in 2020 to 2021 would not count against the maximum amount that may be contributed in 2021 (up to $10,500), and the entire balance of $15,500 could be excluded from tax, if used for dependent care benefits.

Dollar limit increase and non-calendar-year plans

The ARPA increased the allowable amount an individual may contribute to a DC FSA to $10,500 (half that amount in the case of a married individual filing separately) for the individual's 2021 taxable year *(not the plan year).* This has resulted in many questions for *non-calendar-year* DC FSAs. In response, the notice provides examples of the tax consequences due to the changes in the law for both calendar- and non-calendar-year DC FSAs.

In the case of a DC FSA offered under an Internal Revenue Code section 125 cafeteria plan with a *non-calendar plan year* beginning in 2021 and ending in 2022, the increased exclusion amount will not apply to the reimbursement of expenses incurred during the *2022 portion* of the plan year.

The notice provides examples of the tax consequences due to the changes in the law for both calendar- and non-calendar-year DC FSAs.

If more than $5,000 is reimbursed from the DC FSA, the portion of the employee's contribution to the DC FSA for the 2021 plan year that is used to reimburse expenses incurred during the 2022 taxable year may become *taxable*.

The guidance in the notice does not apply to unused DC FSA benefits from one taxable year (typically the calendar year) used to reimburse expenses incurred in the immediately following taxable year, where the expenses are incurred during the same non-calendar plan year spanning those two taxable years, because they are *not* carryover benefits or benefits available under an extended claims period.

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News in Brief

COVID-19 vaccine for adolescents added to preventive care guidelines

By Maureen Gammon and Kathleen Rosenow

On May 10, 2021, the Food and Drug Administration (FDA) issued an Emergency Use Authorization (EUA) for the Pfizer-BioNTech COVID-19 vaccine in adolescents age 12 to 15. Two days later, the Advisory Committee on Immunization Practices (ACIP) of the Centers for Disease Control and Prevention issued an interim recommendation for use of the Pfizer-BioNTech COVID-19 vaccine in adolescents age 12 to 15 for the prevention of COVID-19.

Non-grandfathered group health plans must begin to cover the Pfizer-BioNTech COVID-19 vaccine for adolescents age 12 to 15 with no cost sharing by June 3, 2021.

In accordance with **interim final regulations** issued in October[1] by the Departments of Labor, Health and Human Services, and Treasury, non-grandfathered group health plans must cover qualifying COVID-19 preventive services, including any vaccine and its administration, without cost sharing, within 15 business days (not including weekends or holidays) of a recommendation from the United States Preventive Services Task Force or ACIP.

To date, the FDA has issued EUAs, with the ACIP subsequently issuing interim recommendations, for the Pfizer-BioNTech COVID-19 vaccine (for persons age 16 or older), the Moderna COVID-19 vaccine and the Johnson & Johnson vaccine.[2]

Non-grandfathered group health plans are required to cover the Pfizer-BioNTech (for persons age 16 or older), Moderna and Johnson & Johnson COVID-19 vaccines with no cost sharing effective January 5, January 12 and March 19, 2021, respectively.

[1] See "**Regulations on COVID-19 vaccine and testing requirements issued**," *Insider*, November 2020.

[2] See "**Third COVID-19 vaccine added to preventive care guidelines**," *Insider*, March 2021.

IRS to prioritize large pension plan late commencement issues

By Stephen Douglas, Bill Kalten, Drew Kusner, Laura Roos and Maria Sarli

The IRS's Tax Exempt & Government Entities Division recently released compliance initiatives for the 2021 fiscal year on its **Compliance Programs and Priorities** webpage. Among other things, it is planning to prioritize examinations of required minimum distributions (RMDs) in large defined benefit plans. Few details were provided, but the IRS noted that "[f]ailure to make these distributions could cause plan disqualification as well as a 50% excise tax on amounts not distributed."

In early 2016, the Department of Labor (DOL) rolled out an initiative to investigate large defined benefit plans to determine whether the plan administrator had a process in place to locate and pay benefits to terminated vested participants at the plan's required commencement date. The DOL has identified significant noncompliance and recovered more than $4 billion (between fiscal year 2017 and fiscal year 2020).

Now, the IRS has entered the arena. To get ahead of a potential IRS audit, plan sponsors should consider taking the following actions:

- **Confirm the plan's required commencement date.** Although the IRS compliance initiative targets failures to pay benefits following a participant's attainment of the "required beginning date" under the tax code, the DOL has been enforcing a plan's required commencement date in plan audits. For example, many plans require commencement at a participant's normal retirement date if the participant is no longer employed.
- **Review participant and beneficiary data and identify any individuals beyond their required commencement date.**
- **Search for any such individuals who are missing.** The IRS previously issued a **field directive** on missing participants and the RMD standards under the tax code. The memo directs employee plan examiners not to challenge a qualified plan for its failure to commence or make RMDs to a missing participant or beneficiary if the plan has taken appropriate steps to locate the individual.
- **Correct for any located participant or beneficiary whose benefit did not timely commence.** Correcting late commencement failures before they are identified by a DOL or IRS auditor may significantly reduce penalty exposure.

Correcting late commencement failures before they are identified by a DOL or IRS auditor may significantly reduce penalty exposure.

More generally, plan sponsors should take the following actions if they have not done so already:

- **Review administrative procedures for locating missing participants and for ensuring the timely payment of benefits.** Revise as necessary to reflect recent DOL guidance on missing participant best practices.[1]
- **Review all other terminated vested participant data and correct any data deficiencies.** Going forward, records should be audited on a regular basis (e.g., annually) to ensure contact information is current.

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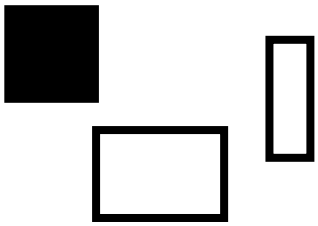

[1] See "**DOL issues guidance on missing participants**," *Insider*, April 2021.

House committee approves SECURE 2.0

By Ann Marie Breheny and Gary Chase

The House Ways and Means Committee unanimously approved the bipartisan **Securing a Strong Retirement Act** (SSRA) (H.R.2954) by a voice vote on May 5. The SSRA, also commonly called SECURE 2.0 because it follows and builds upon the Setting Every Community Up for Retirement Enhancement (SECURE) Act of 2019, is a wide-ranging, bipartisan bill that is intended to increase retirement savings, encourage plan sponsorship, and simplify plan administration and compliance.[1] The legislation is now cleared for a vote on the House floor, though the timing for House floor consideration is not yet clear.

The Senate is expected to consider similar legislation developed by Sens. Ben Cardin (D-MD) and Rob Portman (R-OH). Bipartisan support, the pending retirements of Rep. Brady and Sen. Portman, and other factors are raising expectations that retirement security legislation will be enacted during the 2021 – 2022 legislative term.

Overview of key SSRA provisions

The SSRA includes dozens of provisions broadly aimed at boosting retirement savings, helping plan participants manage their savings and distributions, and easing plan administration and compliance for plan sponsors.

The legislation aims to increase retirement savings by expanding plan sponsorship and participation and allowing higher catch-up contributions by some older plan participants. Some of the provisions to increase retirement savings include:

- **Mandatory automatic enrollment:** In general, new 401(k) and 403(b) plans would be required to automatically enroll employees with a contribution rate of 3% to 10% of compensation and increase the contribution rate by one percentage point annually up to at least 10% (and not more than 15%) of compensation.
- **Higher catch-up contribution limit for individuals age 62 to 64:** The annual catch-up contribution limit, which is currently $6,500 ($3,000 in SIMPLE plans and SIMPLE IRAs) would be increased to $10,000 ($5,000 in SIMPLE plans and SIMPLE IRAs) for employees who are age 62 to 64.
- **Matching contributions on student loan payments:** Employers would be permitted to make matching retirement plan contributions based on an employee's qualified student loan payments.

The bipartisan bill is intended to increase retirement savings, encourage plan sponsorship, and simplify plan administration and compliance.

- **Reduced tenure for part-time employee eligibility:** Part-time employees would be eligible to participate in employer-sponsored defined contribution plans after they have completed 500 hours of service for two consecutive years (rather than three consecutive years as required under the SECURE Act).
- **403(b) MEPs and PEPs:** SECURE Act provisions regarding multiple employer plans (MEPs) and pooled employer plans (PEPs, a type of open MEP) would be extended to 403(b) plans, thus permitting 403(b) PEPs and providing relief from the "one bad apple rule" (under which a violation by one employer would not affect the tax treatment of employees of compliant employers) to 403(b) MEPs and PEPs.
- **Small immediate financial incentives for plan participation:** Employers would be permitted to offer de minimis financial incentives, such as small gift cards, to encourage participation in 401(k) and 403(b) plans.
- **Retirement savings lost and found:** Treasury would be directed to establish a national database to help workers locate retirement benefits from former employers.
- **Saver's Credit:** The Treasury secretary would be directed to take steps to increase public awareness of the Saver's Credit.

Other provisions are intended to help plan participants manage their retirement savings and preserve income during retirement. The legislation also includes provisions addressing access to retirement savings before retirement, such as in cases of domestic abuse. Some provisions addressing retirement income and plan distributions include:

- **Increase age for beginning RMDs:** The required beginning date for required minimum distributions (RMDs) would be 73 for distributions required to begin in 2022 and would gradually increase to 75 beginning in 2032.
- **Remove RMD barriers for life annuities:** Life annuities with certain features, such as certain annual increases, lump sum return of premium death payments and other features, would be permitted in defined contribution plans and IRAs.

[1] Two additional documents related to the legislation are available: **Ways and Means Committee section-by-section summary** and **Joint Committee on Taxation technical description.**

- **Qualifying longevity annuity contracts:** To help employees purchase qualifying longevity annuity contracts (QLACs), the SSRA would repeal a provision that limits QLAC premiums to 25% of a participant's account balance, facilitate QLACs that allow spousal survivor rights and make other changes.
- **403(b) plan investment in collective investment trusts:** Contributions to 403(b) custodial accounts could be invested in collective investment trusts if certain requirements are satisfied.
- **Recovery of plan overpayments:** Plan fiduciaries would have additional flexibility to elect not to recover overpayments mistakenly made to retirees. In addition, limits would be imposed on the amount that a plan fiduciary could recover from a participant or beneficiary, and rollovers of overpayments would remain valid.
- **Reduced penalty for failure to take minimum distributions:** The excise tax for failure to take minimum distributions would be reduced from 50% to 25%. If a failure to take a RMD from an IRA is corrected in a timely manner, the excise tax would be reduced to 10%.
- **Eliminate the 457(b) "first day of the month" requirement:** Participants in a 457(b) plan would be permitted to request changes in their deferral rate prior to the date that the compensation being deferred is available (rather than prior to the beginning of the month in which the deferral will be made).
- **Distributions to firefighters:** The legislation would provide that private sector firefighters who terminate employment and commence payment after age 50 are not subject to the 10% early distribution excise tax, which is the same rule that applies to qualified public safety employees.
- **Repayment of qualified birth and adoption distribution:** Repayment of qualified birth or adoption distributions would have to be made within three years of the date the distribution was received. The SECURE Act, which authorized the distributions, did not limit the repayment period.
- **Domestic abuse withdrawals:** The legislation would permit penalty-free withdrawals in the case of domestic abuse.

Many provisions address plan administration and compliance, including provisions to expand voluntary correction of some plan errors, provisions related to reporting and disclosure and other provisions:

- **Self-correction of inadvertent violations:** In general, inadvertent plan violations could be self-corrected under the Employee Plans Compliance Resolution System (EPCRS) without a submission to the IRS if the self-correction occurs before the IRS discovers the violation on audit.
- **Safe harbor for corrections of certain employee elective deferrals:** The legislation would establish a grace period to correct automatic enrollment and automatic escalation errors without penalty if corrected within nine and a half months after the end of the year in which the mistake occurred.
- **Report to Congress regarding reporting and disclosure requirements:** Treasury, the Department of Labor (DOL) and the Pension Benefit Guaranty Corporation (PBGC) would be directed to review current reporting and disclosure requirements for retirement plans and make recommendations to Congress to consolidate, simplify and improve the requirements.
- **Disclosure relief for unenrolled employees:** Defined contribution plans would not be required to provide notices to unenrolled participants, except for an annual reminder that the individual is eligible to participate in the plan and any otherwise required notice requested by the employee.
- **Annual paper benefit statement:** Unless the participant requests otherwise, defined contribution plans would be required to provide at least one paper benefit statement per year, and defined benefit plans would have to provide at least one paper statement every three years.
- **Top-heavy testing:** If a plan covers employees who are otherwise excludable under the general age and service rules and the employees separately meet the top-heavy minimum contribution rules, the employees may be excluded from consideration in determining if the plan (or any plan of the employer) satisfies the top-heavy rules.
- **Statute of limitations:** The statute of limitations for taxes for prohibited transactions, excess contributions or RMD failures would begin on the date the income tax return is filed for the year the violation occurred (or the date the return would have been due if a return is not required). This would provide relief from situations where the statute of limitations does not start to run because the taxpayer was unaware of an issue and so never filed a return.
- **Self-certification of hardship:** Employees would be permitted to self-certify that an event constitutes a hardship for purposes of hardship withdrawals. In addition, the legislation would codify the current rule that permits self-certification that the amount of a distribution does not exceed the need.
- **Family attribution rules:** For purposes of determining whether two or more businesses must be aggregated for certain non-discrimination tests, ownership by family members is attributed to other family members. The legislation would make changes to these attribution rules, including by disregarding community property laws.

- **Retroactive plan amendments:** Certain retroactive plan amendments that increase benefits (other than matching contributions) for a year could be made by the due date of the employer's tax return for the year.
- **Expanded hardship rules for 403(b) plans:** Currently, hardship distributions for 403(b) plans are generally limited only to employee contributions (excluding earnings). The legislation would allow 403(b) plans to make all amounts available for hardship distributions.
- **Missing participants:** The legislation would direct the DOL to issue regulations outlining steps plan fiduciaries must take to satisfy their fiduciary duties in trying to locate missing participants. In addition, it would increase the cash-out limit to $6,000.

To help raise revenue to offset the cost of some other provisions in the legislation, the SSRA would expand the use of Roth contributions:

- **Mandatory Roth treatment for catch-up contributions:** Catch-up contributions to 401(k), 403(b) and governmental 457(b) plans would be required to be made on a Roth basis.
- **Matching contributions may be made on a Roth basis:** Employers may permit employees to elect for their matching contributions under 401(k), 403(b) and governmental 457(b) plans to be made fully or partially on a Roth basis.

The legislation also includes provisions addressing small employer tax credits, IRAs, technical corrections to the SECURE Act and other changes.

Next steps

The legislation is now cleared for a vote on the House floor, though the timing for floor action has not been announced. Senate attention is also expected. During the 2019 – 2020 legislative session, Sens. Ben Cardin (D-MD) and Rob Portman (R-OH) sponsored legislation that was similar to the SSRA and shared some key provisions. They are expected to introduce the legislation again this year, and Senate action on retirement savings seems likely. Upcoming budget reconciliation legislation could provide a vehicle for moving SSRA and related provisions through Congress.

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News in Brief

CMS issues OOPM limits, guidance on COBRA subsidies/ marketplace SEPs

By Anu Gogna and Ben Lupin

The U.S. Department of Health and Human Services (HHS) and the Centers for Medicare & Medicaid Services (CMS) have issued the final **Notice of Benefit and Payment Parameters for 2022** and accompanying **Fact Sheet**.

The notice addresses a variety of Affordable Care Act (ACA) benefit provisions that go into effect in 2022 and affect both the group and individual health plan markets. While much of the guidance in the notice does not directly apply to employers that sponsor large self-insured and fully insured group health plans, the notice does include the following:

1. **The 2022 annual dollar limits on cost sharing,** which are $8,700 for individual coverage and $17,400 for family coverage (up from $8,550 and $17,100, respectively, for 2021).
2. **Guidance on special enrollment periods (SEPs) on the public marketplace due to the end of COBRA subsidies.** Individuals enrolled in COBRA continuation coverage may qualify for a SEP – a period when individuals are eligible to enroll in marketplace plans outside of annual open enrollment – to enroll in individual health insurance coverage *on or off the public exchange* due to the *complete cessation* of employer contributions or government subsidies to COBRA continuation coverage (such as those provided for under the American Rescue Plan Act of 2021[1]). Note: HHS is considering whether situations where an employer *reduces, but does not completely cease,* its contributions for COBRA continuation coverage could result in a marketplace SEP. Future guidance might address this issue.

[1] See "**Health and benefit implications of ARPA**," *Insider*, March 2021.

WTW Pension 100: Year-end 2020 disclosures of funding, discount rates, asset allocations and contributions

By Brendan McFarland

Despite another year of strong investment performances witnessed by plan sponsors over the past decade, the aggregate funded status[1] of defined benefit plans in the Willis Towers Watson (WTW) Pension 100[2,3] managed to rise only slightly, from 87.1% in 2019 to 88.3% in 2020. The year 2020 was tumultuous for pension funding as plan sponsors witnessed volatile financial markets erode 2019 gains over the first quarter of 2020[4] due to the COVID-19 pandemic. Fortunately, by the end of 2020, markets rebounded, leaving sponsors with strong returns on their pension plan investments. This coupled with employer contributions helped boost plan assets; however, lower interest rates increased plan liabilities, offsetting a significant portion of the investment gains witnessed over the year.

This annual analysis[5] is based on just-reported pension disclosures from the Securities and Exchange Commission (SEC) 10-K filings of 100 publicly traded U.S. sponsors of large pension plans whose fiscal years end in December. We examine reported funding results, the discount rates used to measure liabilities, target asset allocation policies over time, investment returns and plan contributions. Where applicable, historical values are shown for companies in the current WTW Pension 100.

Among these WTW Pension 100 plans, the gap between liabilities and assets has widened substantially. Between 2007 and 2012, funding dropped from a $67 billion surplus to a $291 billion deficit – the largest deficit in our analysis (Figure 1). The deficit has been slow to improve since 2012, even with favorable investment performances and years of strong employer contributions, mostly due to the continuous decline in interest rates used to measure pension obligations.

This phenomenon repeated itself over 2019 and 2020, as once again both plan assets and obligations moved in tandem. This time around, sponsors witnessed historically low interest rate levels for two years in a row, which were offset by the strong investment gains witnessed during this period of analysis, pushing up funding ratios ever so slightly for the fourth year in a row (albeit with very little change in the aggregate deficit).

[1] The aggregate funded status is the ratio of (a) the sum of all assets to (b) the sum of all projected benefit obligations (PBOs) for the 100 companies. Average funded status is calculated by averaging the ratio of (a) to (b) on an individual company basis.

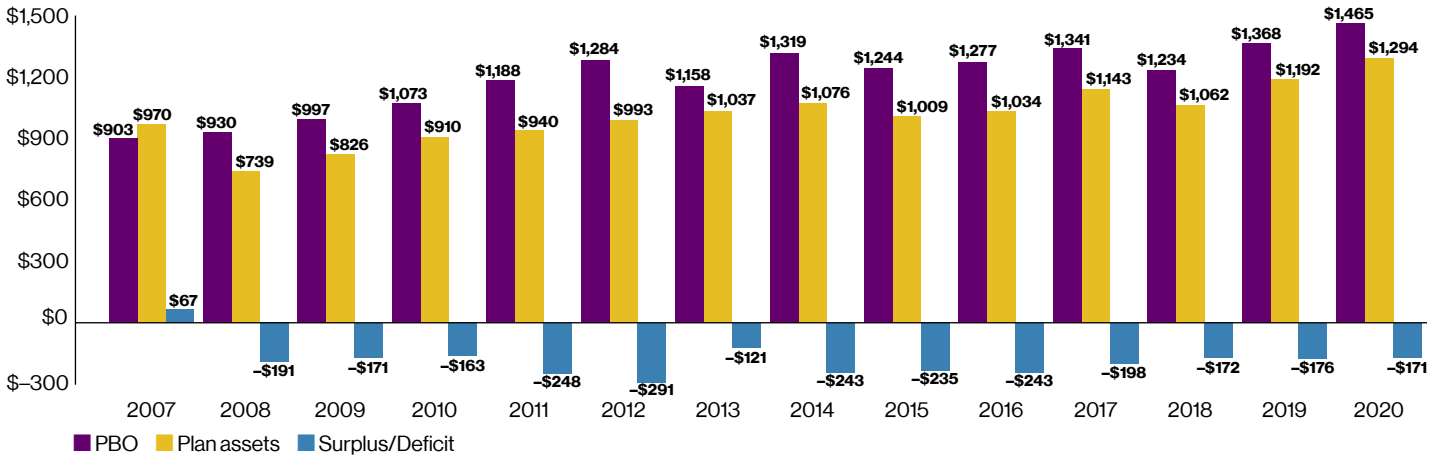
[2] The 2020 WTW Pension 100 consists of sponsors of the largest U.S. pension programs among U.S. publicly traded organizations, ranked by PBO at year-end 2019. For some companies, the allocation between U.S. and non-U.S. plans is estimated.

[3] Pension liability values in 10-Ks also reflect nonqualified plans (which are usually not shown separately). An analysis of companies that disclose their qualified and nonqualified plans separately found that funded status is typically seven percentage points higher without the nonqualified plan obligations because these plans are typically not funded.

[4] See "**COVID-19 takes bite out of U.S. corporate pension plan**," April 2, 2020

[5] See "**WTW Pension 100: Year-end 2019 disclosures of funding, discount rates, asset allocations and contributions**," *Insider*, April 2020

Figure 1. **Aggregate funding levels for WTW Pension 100 ($ billions), 2007 – 2020**



Source: Willis Towers Watson

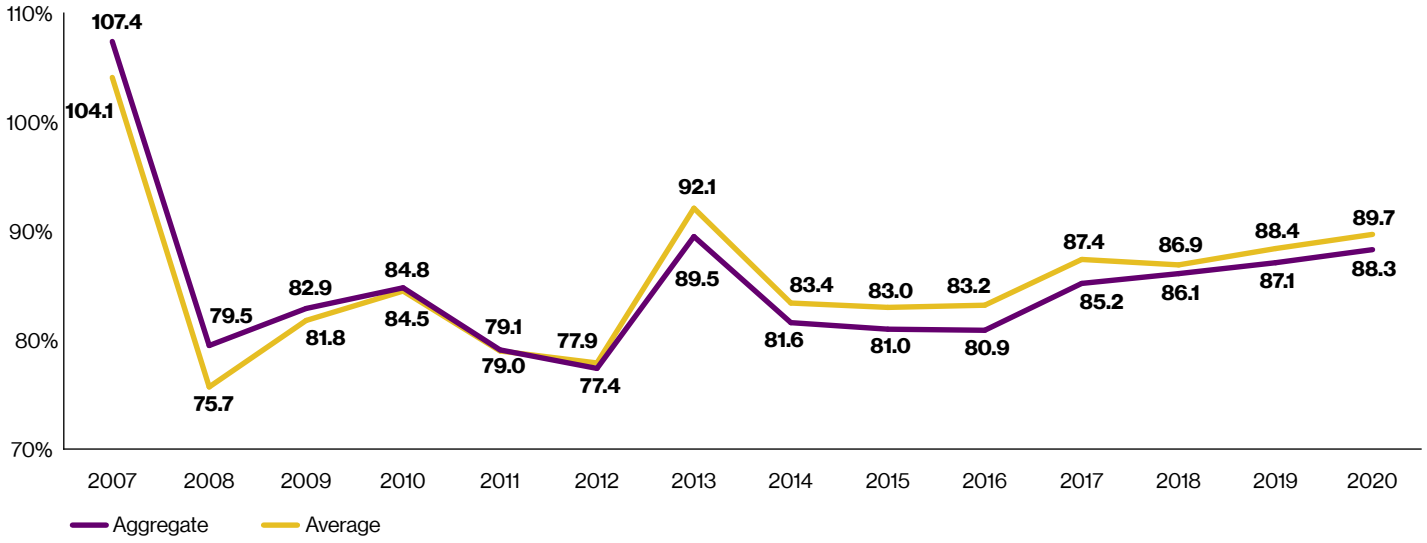
Funded status increases for the fourth year in a row

Among WTW Pension 100 companies, plan obligations increased by 7% in 2020, while plan assets increased by roughly 9%. While funded status improved, the overall deficit decreased minimally by $5 billion – from $176 billion to $171 billion – a 3% decrease over the year. The overall deficit declined by $120 billion between its peak in 2012 and 2020, as investment returns and employer contributions outpaced the growth in liabilities associated with declining interest rates. Among these same companies, aggregate funded status climbed to 88.3% by the end of 2020, up from 87.1% in 2019, 86.1% in 2018 and 85.2% in 2017 (Figure 2). Over the past year, average funded status also witnessed an increase, moving from 88.4% at the end of 2019 to 89.7% at the end of 2020.

While funding levels improved for most over the year, companies are still nowhere near 2007 levels.

Figure 3 shows the distribution of funded status since 2007, reflecting some significant shifts over the analysis period. The number of companies whose funded status was 90% and greater increased from 42% in 2019 to 49% in 2020. On the other end of the spectrum, funding levels were below 70% for seven companies in 2020, compared with five companies in 2019. While funding levels improved for most over the year, companies are still nowhere near 2007 levels, when 75% of companies in this analysis had funding levels that were 90% or greater.

Figure 2. **Aggregate and average funded status for WTW Pension 100, 2007 – 2020**



Source: Willis Towers Watson

Figure 3. **Distribution of funded status for WTW Pension 100, 2007 – 2020**

	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
100% or more	**51%**	**5%**	**8%**	**9%**	**7%**	**6%**	**23%**	**7%**	**7%**	**8%**	**15%**	**13%**	**13%**	**16%**
90% to 99%	**25%**	**11%**	**11%**	**17%**	**8%**	**11%**	**25%**	**18%**	**14%**	**15%**	**26%**	**23%**	**29%**	**33%**
80% to 89%	**16%**	**19%**	**32%**	**37%**	**26%**	**22%**	**32%**	**33%**	**36%**	**33%**	**28%**	**35%**	**31%**	**27%**
70% to 79%	**5%**	**28%**	**30%**	**26%**	**31%**	**33%**	**31%**	**32%**	**31%**	**28%**	**21%**	**20%**	**22%**	**17%**
Under 70%	**3%**	**37%**	**19%**	**11%**	**28%**	**28%**	**4%**	**10%**	**12%**	**16%**	**10%**	**9%**	**5%**	**7%**

Source: Willis Towers Watson

Figure 4 shows the changes in funded status from 2019 to 2020. As noted earlier, average funded status improved over 2020. On a company basis, funded status improved for 67 sponsors and declined for 33. The funding increases were between 0.1 and 4.9 percentage points for 57 companies and were five percentage points or more for another 10 companies (owing to large plan contributions explained later in this study).

Discount rates continued to drop even further in 2020

Plan obligations increased by roughly 7% in 2020, mostly due to a decline in discount rates used to measure pension obligations. From 2008 through 2012, discount rates fell every year — an accumulated decline of 234 basis points — before finally rising in 2013 (Figure 5). Interest rates fluctuated between 2013 and 2018. By the end of 2019, rates again plummeted as sponsors witnessed the largest one-year drop over the period of this analysis. During 2020, rates continued this trend and fell even further by an additional 72 basis points, leaving sponsors at a new historically low average rate of 2.56%.

Gradual shift to more conservative investments continues

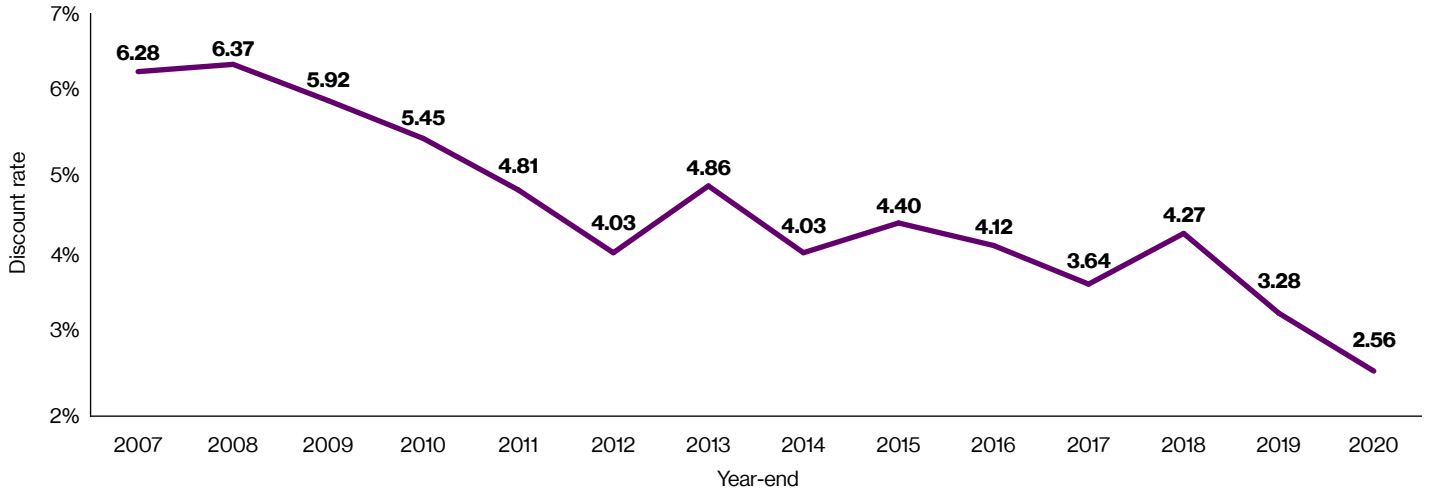
Over the past decade, a gradual shift from public equities to fixed-income and alternative assets reflects growing interest in hedging funded status and reducing market risk exposure (Figure 6). Since 2009, the average target allocation to public equities declined by close to 19 percentage points, while target allocations to fixed-income investments rose by around 16 percentage points.

Figure 4. **Changes in funded status for WTW Pension 100, 2019 – 2020**

Change in funded status over the year	Number of companies	Average change in funded status
5.0% or more	**10**	**9.1%**
0.0% to 4.9%	**57**	**2.1%**
–0.1% or less	**33**	**–2.6%**
Total	**100**	**1.3%**

Source: Willis Towers Watson

Figure 5. **Average year-end discount rate assumptions for WTW Pension 100, 2007 – 2020**



Source: Willis Towers Watson

Figure 6. **Average target asset allocation percentages for WTW Pension 100, 2009 – 2021***

	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2021 (aggregate)
Public equity	**54.7%**	**52.4%**	**50.5%**	**47.1%**	**45.7%**	**43.3%**	**42.8%**	**42.6%**	**42.3%**	**40.9%**	**38.6%**	**37.3%**	**36.2%**	**32.5%**
Fixed income	**34.3%**	**34.7%**	**36.0%**	**38.9%**	**40.0%**	**42.3%**	**42.9%**	**43.3%**	**43.4%**	**45.3%**	**47.7%**	**48.5%**	**50.0%**	**50.4%**
Cash	**0.3%**	**0.7%**	**0.9%**	**0.8%**	**0.9%**	**0.9%**	**0.9%**	**0.9%**	**1.0%**	**1.0%**	**1.1%**	**1.4%**	**1.3%**	**1.3%**
Real estate	**3.2%**	**3.3%**	**3.0%**	**3.0%**	**3.0%**	**3.0%**	**3.1%**	**3.2%**	**3.2%**	**3.1%**	**3.0%**	**3.4%**	**3.2%**	**4.6%**
Other	**7.5%**	**8.9%**	**9.6%**	**10.3%**	**10.4%**	**10.6%**	**10.3%**	**10.1%**	**10.1%**	**9.7%**	**9.7%**	**9.4%**	**9.3%**	**11.3%**

Source: Willis Towers Watson

*Represents investment targets for the oncoming year. Some firms reported their targets in terms of a single value, while others reported a range. If the target allocation was given as a range, we normalized the results. "Other" includes target percentages for private equity, hedge funds, alternative and miscellaneous asset classes when reported.

In 2020, investment returns for plans in the WTW Pension 100 averaged 14.5% (aggregate returns were 14.4%), well above expectations.

The steady shifts to fixed-income holdings between 2008 and 2013 (as reflected in the 2014 target allocation column) slowed during the next few years but then picked back up again over 2017 and 2018 (reflected in the 2018 and 2019 columns). On average, fixed-income holdings increased by 2% going into 2018 and 3% at the beginning of 2019. Over the past two years, movement slowed relative to previous years as fixed income increased by roughly 1% per year. At the beginning of 2021 (reflected in the 2021 column), on average, half of plan assets for companies were invested in fixed-income instruments.

Out of the 90 companies that reported target asset allocation information for both 2020 and 2021, 11 reduced their target equity allocation by five percentage points or more, with an average reduction of roughly eight percentage points. Among these companies, eight plan on reducing equities and increasing fixed-income holdings, two plan on increasing "other" holdings, while one is shifting from equities into a mix of fixed income and "other."

These recent allocations to fixed income could reflect higher funding levels triggering or accelerating de-risking strategies, such as glide paths, which reduce equity exposure as the plan moves closer to full funding. Only five companies increased their equity exposure by five percentage points or more over the year, with an average increase of seven percentage points.

Similar to past studies, aggregate results (weighted by plan assets) differ from average results going into 2020, which suggests that allocations vary by size. On an aggregate level, sponsors of the largest plans hold less in public equities and more in real estate/other alternative investments, indicating the larger plans in this analysis have more alternative investments than the smallest.

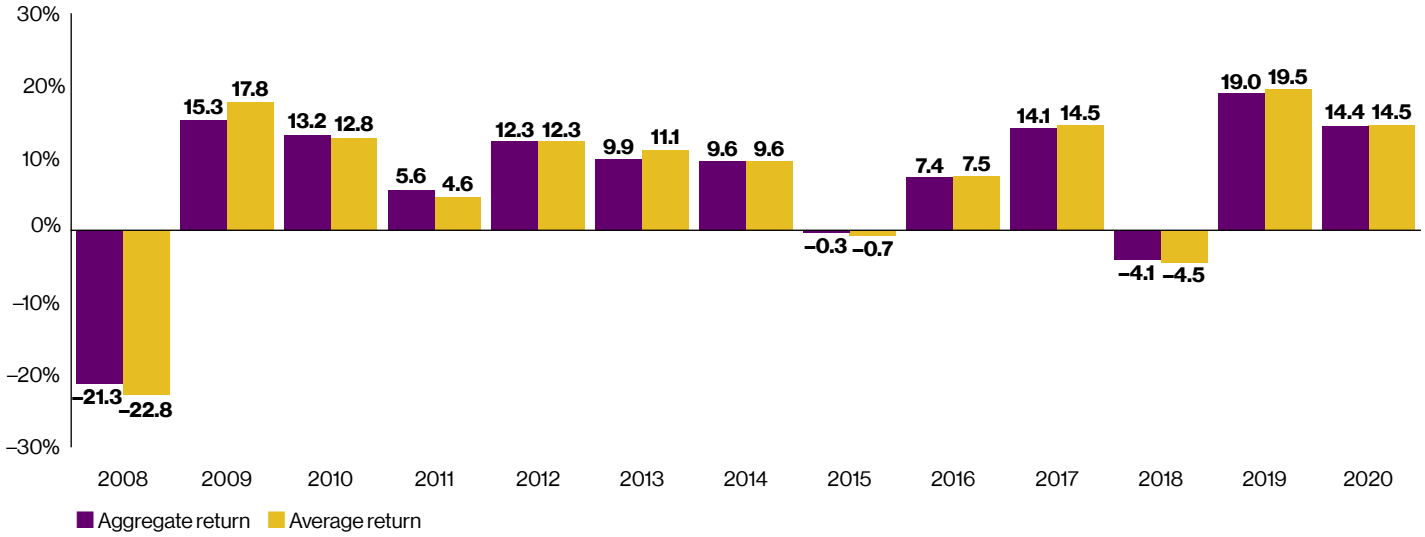
Sponsors realize another strong year for returns on their pension plan investments

2020 was another strong year for plan sponsors in regard to both stock and bond markets. Domestic large capitalization equities grew 18%, while domestic small/mid-capitalization equities realized gains of 20%. At the same time, aggregate bonds recognized gains of 8%, while long corporate and long government bonds, typically used in liability-driven investing strategies, realized gains of 13% and 18%, respectively. These strong market performances left sponsors witnessing another fortuitous year of returns and some of the strongest realized over the period of our analysis (Figure 7).

In 2020, investment returns for plans in the WTW Pension 100 averaged 14.5% (aggregate returns were 14.4%), well above expectations, which helped drive up plan assets and funding levels over the year.

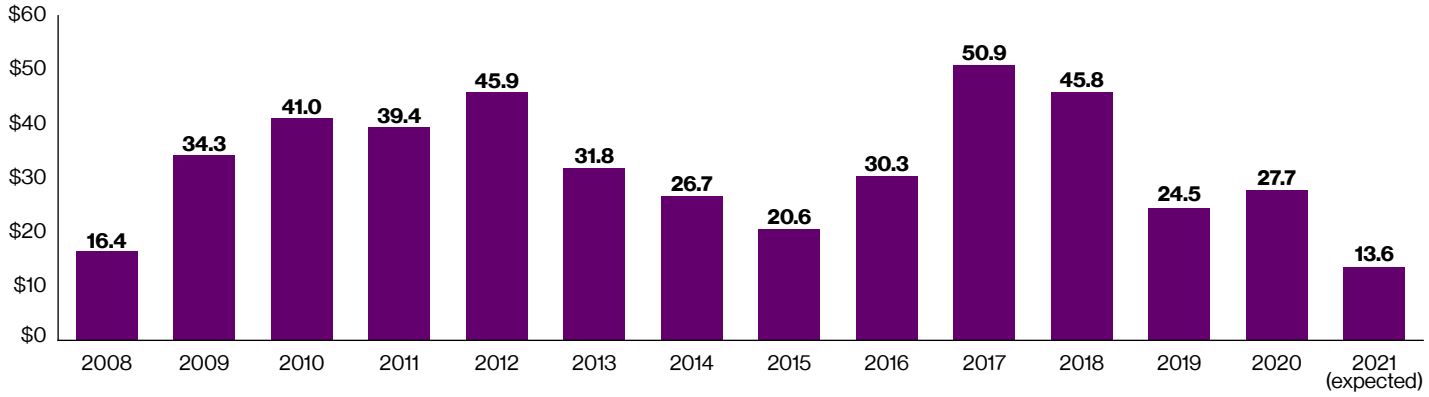
Averaged over the past three years, annualized returns for the WTW pension 100 were 9.3%. Since 2008, annualized investment returns have averaged 6.7% – largely attributed to significant losses in the 2008 financial crisis. Returns averaged 9.6% over the post-financial crisis 12-year period between 2009 and 2020. On average, these plan sponsors' returns outperformed expectations in nine of the past 13 years.

Figure 7. **Investment returns for WTW Pension 100, 2008 – 2020**



Source: Willis Towers Watson

Figure 8. **Plan contributions from WTW Pension 100 ($ billions), 2008 – 2021***



Source: Willis Towers Watson
*The 2021 employer contribution column reflects expected contributions to be provided by sponsors over 2021 as disclosed in 10-K annual reports.

Contributions in aggregate increased over 2020

WTW Pension 100 companies contributed $27.7 billion in 2020 – up 13% from 2019 (Figure 8). Aggregate contributions in 2017 and 2018 were the highest realized in this analysis, during a time when sponsors were responding to rising Pension Benefit Guaranty Corporation premiums, the attractiveness of borrowing to fund pensions, growing interest in de-risking strategies and a desire to prefund future contributions. Most importantly, the Tax Cuts and Jobs Act of 2017 reduced federal corporate tax rates starting in 2018 and, as a result, increased the relative value of the pension tax deduction for earlier tax years. Plan contributions normalized in 2019 and 2020 as sponsors benefitted from the flexibility provided by prefunding contributions.

Aggregate contributions were 1.6 times aggregate service cost,[6] which was $17.7 billion in 2020.

While aggregate contributions were up in 2020 compared with 2019, only a little more than one-third of plan sponsors made larger contributions than what was contributed in 2019 (Figure 9), as several large sponsors made sizeable contributions over the past year. Ten companies were responsible for roughly 60% of WTW Pension 100 employer contributions in 2020. Under the Coronavirus Aid, Relief, and Economic Security (CARES) Act, sponsors were able to defer the timing of their pension payments owed for 2020, providing them with flexibility to make their payments at any time during 2020 or the beginning of 2021.

Only one company in this analysis ended up deferring its minimum required pension contribution until the beginning of January 2021 due to the CARES Act. A handful of sponsors did not have a required minimum contribution in 2020 but publicly stated that due to COVID-19 they were not making discretionary contributions in 2020 – contributions that would have been substantial based on previous expectations set at the beginning of last year. This downtick in discretionary funding is likely to continue into 2021, as expected contributions for this year are relatively low compared with prior-year contribution levels.

Most companies whose funded status increased substantially during 2020 did make relatively large plan contributions. Among companies whose funding levels rose by more than five percentage points, the average ratio of plan contributions to plan assets was 8%, compared with 2% for the entire WTW Pension 100.

[6] Service cost refers to the present value of the projected retirement benefits earned by plan participants in the current period.

Figure 9. **Plan contributions ($ billions) from WTW Pension 100, 2019 versus 2020**

	Number of companies	Aggregate contributions in 2019	Aggregate contributions in 2020
Larger contributions in 2020	**36**	**$7.3**	**$20.9**
Same level of contributions in 2019 and 2020	**13**	**$0.1**	**$0.1**
Smaller contributions in 2020	**51**	**$17.1**	**$6.7**

Source: Willis Towers Watson

Under the CARES Act, sponsors were able to defer the timing of their pension payments owed for 2020.

Funding levels continue to increase over the first quarter of 2021

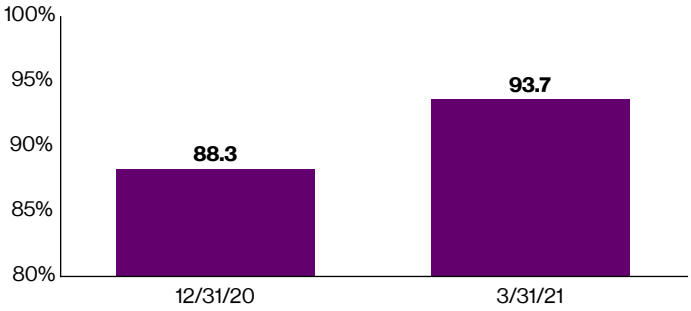
Over the first quarter of 2021, the aggregate of WTW Pension 100 companies experienced an increase in funded status. Aggregate funded status for this selection of companies was estimated to jump up by 5.4 percentage points to 93.7% by the end of March, the highest levels witnessed since 2007 (Figure 10).

During the first quarter of 2021, interest rates used to measure pension obligations started to rebound from previously historically low levels (an increase of 69 basis points from end of December 2020 to end of March 2021), driving down plan obligations.

As more plan sponsors have adopted liability-hedging strategies, rising interest rates have corresponded to negative fixed-income returns and overall negative investment returns, in aggregate (–1.5% for companies in this analysis). However, not all sponsors are fully hedged, and aggregate funded status is therefore expected to benefit from rising interest rates as well as positive returns from equity markets.

This rise in estimated funding levels is projected to cut the deficit realized at the end of 2020 in half (roughly $85 billion) by the end of the first quarter of 2021.

Figure 10. **Estimated aggregate funded status for Q1 2021, WTW Pension 100**



Source: Willis Towers Watson

Conclusion

Over 2020, while sponsors watched interest rates used to measure their pension obligations drop to new historical levels for the second year in row – driving up plan liabilities – they were fortunate to ride another wave of strong financial markets, leaving their pension plans in slightly better funding positions than what was realized for the fourth year in a row.

Over the first three months of 2021, funding outcomes have been more prosperous for plan sponsors as interest rates have started to rebound from prior levels, leading to significant declines in pension obligations. Even though bond market returns have been negative during the same time frame, growth/return-seeking assets have been positive, leaving sponsors with slightly negative investment returns, reducing plan assets minimally. This combined effect is expected to drive funding levels up significantly by the end of the first quarter of 2021, potentially wiping out half of the deficit realized at the end of 2020 and putting sponsors one step closer to being fully funded.

The American Rescue Plan Act (ARPA) passed in March 2021 contains provisions applicable to pension funding, including further extension of interest rate stabilization and an extension of the amortization period for funding shortfalls to 15 years (up from seven previously). For plans that are underfunded, these provisions will serve to reduce near-term contribution requirements and provide a longer time horizon for funding the remaining pension deficit.

In light of the rapid improvement in funded status and the changes in funding requirements provided under ARPA, plan sponsors have an opportunity to reconsider their financial management strategies. We anticipate that sponsors will revisit their funding, investment and settlement strategies in 2021 to reflect improved funding levels and additional flexibility provided by the changes in funding rules.

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INSIDER-2021-05