It's All About the Beneficiaries

Fiduciary Handbook for Understanding and Selecting **Target Date Funds**

John Lohr, Mark Mensack & Ron Surz

Understanding and Selecting Target Date Funds

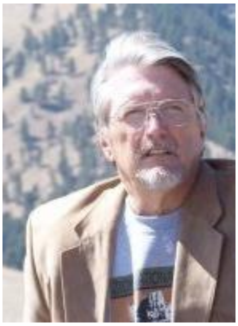
Preface

Target date funds are a *good idea* that could become a *great idea*. It wouldn't take much more to do what is best for beneficiaries. This handbook is normative. It explains what should be provided by target date funds.

Each Chapter has 3 sections:

1. **Statement of facts** written by Ronald Surz, President and CEO of Target Date Solutions. During Ron's 40 years of pension consulting he has advised several $ trillions, primarily on asset allocation and investment policy. He wrote the educational book on investment policy for Certified Investment Management Analysts (CIMAs). Ron is the sub-advisor of the SMART Fund Target Index offered by Hand Benefit and Trust, Houston.

2. **Legal guidance** written by John Lohr, independent ERISA attorney and author. During his 40-year career, John has served as corporate counsel to E.F. Hutton and Lockwood Financial Group and has committed to improving the financial literacy of the



investing public and their investment professionals. John's most recent endeavors include the introduction of "Fiduciary Forensics."

3. 

   <u>Ethical Perspective</u> written by Mark Mensack, Chief Ethics Officer of Mark D. Mensack, LLC. Prior to his 19 years in financial services, Mark taught philosophy and ethics at the United States Military Academy. Mark writes the 401k Ethicist column for the ***Journal of Compensation & Benefits***

Many thanks to Sydney LeBlanc for her remarkable editing and Conor Byrnes for his masterful book creation.

Pension Protection Act of 2006

Chapter 1 History

Target date funds (TDFs) were first introduced in the early 1990s by Barclays Global Investors (BGI) and were originally used for college savings plans. The target date, for example the 2020 fund, is an event date. In the case of college savings plans, it's the year that a student intends to enroll in a college. Target date funds' asset allocation mix typically provides exposure to return-seeking assets, such as equities, in early years when risk capacity is higher, and becomes increasingly conservative as time progresses with exposure switched progressively toward capital-preservation assets, such as short-term bonds. This asset movement through time from more to less risk is called a "glide path." Eventually, target date funds began to be used for retirement savings plans, especially 401(k) plans. The event date in this application is the year in which an investor intends to retire.

Usage of TDFs remained minimal until 2006. Two major events brought TDFs to the forefront. First, behavioral scientists recommended that 401(k) plans use automatic enrollment to encourage participation. Employees would need to choose to be excluded from the plan, whereas they formerly needed to sign on for the plan. Behavioral scientists were right. 401(k) participation skyrocketed, but this created a new challenge. Many 401(k) participants were either unable or incapable of making an investment decision so they defaulted to their employers who, typically, placed their contributions in very safe assets, like cash. This led to the second major event: passage of the Pension Protection Act of 2006 (PPA).

Why is the Passage of the Pension Protection Act of 2006 Significant?

The PPA specifies three Qualified Default Investment Alternatives (QDIAs) that plan sponsors can use for participants who do not make an investment election: Target Date Funds, Balanced Funds, and Managed Accounts (accounts managed by outside professionals). By far the most popular QDIA has been TDFs. It's important to remember that most of the assets in TDFs are there by default, so these investments are employer-directed rather than participant-directed. Accordingly, there should be a separate statement of investment policy for each TDF.

Subsequent to the PPA, target date fund assets grew from $0 to about $150 billion in just two short years. This set the stage for serious disappointment in 2008 when the typical 2010 fund lost 25%. The market crash of 2008 exposed the fact that far too much risk was being taken, especially near the target date. Note that the 2010 fund is designed for those retiring between 2005 and 2015. Participants who defaulted their investment decision to their employers believed they were protected, especially near retirement, so they were devastated and shocked. As a consequence of this pathetic loss, the U.S. Securities and Exchange Commission (SEC) and the Department of Labor (DOL) held joint hearings in 2009, and subsequently threatened to regulate TDFs in a variety of ways, specifically by requiring more disclosures. At the time of this writing, these threats remain to be carried out. In the meantime, nothing of consequence has changed since 2008, other than some minor improvements in fees and diversification. The vulnerable participants remain in as much jeopardy today as they were in 2008.

The good news about 2008 is that not much was at stake, with $150 billion in TDFs, which was less than 10% of 401(k) assets. The next 2008 will be devastating by contrast, and it's not a matter of *if* – it's a matter of *when*. At the time of this writing, TDFs hold $1 trillion, which is about 25% of all 401(k) assets.

Legal Guidance

Should fiduciaries rely exclusively on the QDIA safe harbor?

The most severe problem facing plan sponsors is the denial of plausibility. Many believe that because they offer a variety of funds in their 401(k) and they state they wish to comply with 404(c), they're off the hook. The courts are daily proving this thought process wrong.

There have been 522 ERISA-related fiduciary breach cases since late 2013. The significant breaches include self-dealing, imprudent investments, failure to submit contributions, and failure to diversify. The good news for plans with TDFs is that a high percentage of lawsuits deal with excessive fees, so courts have not yet addressed the selection and monitoring of TDFs.

The bad news in the 401(k) world is that plan sponsors and their fiduciaries are liable for the funds that they select for their plan. Sure, following 404(c) can shift liability for selection of investments to participants if certain conditions are met, but default investments are employer-directed rather than participant-directed.

Fiduciaries were unscathed in 2008. Should they expect the same next time?

The only advice we can give plan sponsors is— **Don't be Complacent**. The sole fiduciary criterion in the 401(k) world is to strive for the best outcomes for your participants and their beneficiaries.

Remember that in Barker v. American Mobil Power Corp. 64 F.3d 1397, a court held that a fiduciary had an affirmative duty to inform participants about circumstances that could jeopardize benefits.

So while the class action lawyers are circling the 401(k) chum in the water, it becomes readily apparent that the regulator's traditional solution of "more disclosure" will be woefully inadequate.

Sponsors, be informed, stay educated, be prudent and, where necessary, hire professionals.

Ethical Perspective

Many plan sponsors fail to realize that fiduciary duties are not merely legal responsibilities, but ethical obligations as well. While the legal responsibilities have been described as "the highest known to the law," the ethical obligations affect the retirement income security of tens of millions of Americans. Donovan v. Bierwirth, 680 F.2d 263 (2nd Cir. 1982)

What is the ethical obligation? Plan sponsors have the fiduciary duty to ensure that participants are provided with a 401(k) product that provides a reasonable opportunity to achieve retirement income security. So while the legal motivation to fulfill one's fiduciary duties compare to the proverbial stick, the ethical motivation is the proverbial carrot.

Plato didn't have a 401(k), but in ***The Republic*** he did address the carrot and the stick. Plato tells the story of Gyges, a shepherd employed by the king. One day, there was an earthquake while Gyges was out in the fields, and he noticed that a cave had been uncovered on the side of a mountain. As he investigated, he discovered the tomb of an ancient king, and on the finger of the corpse was a gold ring. He took the ring and soon discovered that it allowed the wearer to become invisible. Gyges realized that if he was invisible, he could do whatever he desired with no fear of punishment. The next time he went to the palace to give the king a report about his sheep, he put the ring on, killed the king, seduced the queen, and ruled the land.

Plato intended this story as an argument for the necessity of laws; however, there's another moral to the story. During every philosophy class at West Point, I would ask my students what they would do today with the ring that they would not have done yesterday. The responses varied from things that would cause the cadet to be expelled from the Academy, to “nothing at all.” The moral is that we often know what ethical course of action we should take to get the carrot, but sometimes a stick is necessary to keep us on track.

Chapter 2
The Duty of Care

By stipulating three Qualified Default Investment Alternatives (QDIAs), the Pension Protection Act of 2006 has established certain forms of safe harbors, but the substance, i.e., the selection of a specific QDIA, remains a fiduciary responsibility. Under the duty of care, fiduciaries must decide which form is most appropriate for their plan and they must strive to select the best they can find. They can't just simply throw darts at the QDIA dartboard.

Most fiduciaries have selected target date funds (TDFs) as their preferred form, but they have not done their utmost to find the best TDF. TDFs have not been vetted. For the most part, assets have been entrusted to the Big 3 bundled service providers – T. Rowe Price, Vanguard and Fidelity. These are fine firms, but the duty of care requires selection on the basis of superiority, rather than on convenience and familiarity.

Fiduciaries Set Objectives That Fulfill the Duty of Care

To select the best, fiduciaries need to establish objectives. What should the TDF achieve? Fiduciaries are duty-bound to seek solutions rather than settling for products. The word "solution" really needs to be taken seriously. The good news is that a universal objective can be achieved with reasonable confidence. This is the objective that fiduciaries should embrace.

Capital preservation is the universal objective of TDFs, the "perfect fit" for this "one-size-fits-all." The Hippocratic Oath of TDFs should be "lose no money." It's the one objective that we all have in common. Of course we all want to earn as much as we can, but we are most impacted by loss as we near retirement. Accordingly, the presumption for target date fund design near the target date should be that participants have saved enough to support a lifestyle that is acceptable to them. Some may plan for a humble lifestyle while others see yachts in their future. It's all the same. A plan is a plan.

Prior to the Pension Protection Act of 2006, the most common investment default was cash, but now the risk pendulum has swung too far for those nearing retirement. 2008 is all the proof we need.

The Center for Due Diligence surveyed investment advisors in 2012 and found that the majority want no risk of loss for those nearing retirement. There is a disconnect between this survey and advisor selections of TDFs with 40-60% in equities at the target date, which is the range for the Big 3.

Fiduciaries need to embrace the capital preservation objective and reject the hopes that are currently being sold. A hope is an objective without a reasonable course of action. Replacing pay and managing longevity risk are hopes because no glide path can realistically be expected to achieve these objectives; rather, saving enough is the right course of action. The main objective of TDFs should be to get the participant safely to the target date with accumulated savings intact. Not everyone agrees with this universal objective, which leads to "The Glide Path Debate" described in Chapter 6 on Current Practices.

Legal Guidance

What are the duties of a fiduciary?

The fiduciaries of a retirement plan have a legal responsibility to manage all aspects of the plan in the best interest of the plan's participants. This means adhering to four core fiduciary standards established by ERISA: to act prudently, and with loyalty to the plan participant, diversifying plan investments, and carrying out plan duties in accordance with plan documents and all relevant laws and regulations:

1. Act Prudently

All plan fiduciaries are expected to act as prudent experts. This means they are to be held to a higher standard of knowledge and informed experience than the average Joe off the street. A plan fiduciary has the responsibilities of a trained professional, and is expected to have a knowledge and capacity in their field suitable for an expert. Fiduciaries have the duty of care while performing any acts that could foreseeably harm others. Good faith, or so-called "empty head and good heart," is not enough. The process that a fiduciary follows and the supporting documentation are critical. There are specific procedures for prudence.

2. Act with Loyalty to the Plan Participants

Fiduciaries must act solely in the interest of plan participants. Decisions for the purpose of corporate or personal gain are strictly prohibited.

3. Diversify Plan Investments

Each plan investment must be considered as part of the plan's entire portfolio. All parts of the whole should fit together in an integrated and well-balanced design.

4. Carry Out Plan Duties in Accordance with Plan Documents and with ERISA

Fiduciaries must be familiar with the plan's governing documents as well as with the standard ERISA requirements.

Once these core standards are understood, the specific issues of the plan can be addressed. Plans are unique. Some have similar characteristics, but each also has its own individual requirements and circumstances. For example, fiduciaries are duty-bound to mitigate investment and administrative expenses. As far as the Department of Labor (DOL) is concerned, if you pay more for a product or a service, it does not necessarily mean that product or service is better. As we said in Chapter 1, fees are a specific witch hunt of the DOL now.

Who are fiduciaries?

In simple terms, all parties with discretionary authority or control over the management of the plan are fiduciaries.

What can often be confusing about fiduciary status is that the same party frequently holds multiple roles. For example, in most plans, the sponsor is both the Named Fiduciary and the 3(16) Plan Administrator. All fiduciary liability for the plan originates with the Named Fiduciary. There is no reduction in the sponsor's liability by delegation to the 3(16) Administrator, because the Administrator is usually the sponsor.

Management and disposition of the assets is the area with the most exposure to liability, and is often delegated. If investment matters are delegated to a skilled professional such as a registered investment adviser who acknowledges its fiduciary responsibility, then the named fiduciary will not be responsible for the day-to-day portfolio management activities, PROVIDED that the delegation has been made with those same prudent standards.

What happens when duties are breached?

Liability for breach of fiduciary responsibility is harsh and personal. Under the statutes, “Any person who breaches any of the responsibilities, obligations or duties imposed upon fiduciaries shall be personally liable to make good to such plan any losses to the plan resulting from such breach.” Personal liability can include fines, civil penalties, and other penalties. ERISA imposes a penalty of 20 percent of the amount recovered by the DOL from a fiduciary who breaches their fiduciary duty or commits another violation of ERISA, such as a prohibited transaction. A qualified plan is required to pay a 15 percent excise tax every year until it corrects the transaction.

Fiduciaries that do not follow the required standards of conduct are personally liable. If the plan lost money because of a breach of their duties, fiduciaries have to restore those losses, plus any profits received through their improper actions. For example, if an employer did not forward participants' 401(k) contributions to the plan, the employer would have to pay back the contributions to the plan as well as any lost earnings, and return any profits they improperly received.

Ethical Perspective

Many of the words found in the legal guidance above, such as prudence, loyalty and care, are also used in these ethical perspectives. That is because those who created ERISA recognized that neither a rule-based system of laws nor principle-based ethical theories were sufficient to protect the American worker's prospects of retiring with dignity.

For centuries, philosophers have debated the pros and cons of a rule vs. principle approach to ethical theory. Rules, like the letter of the law, can be inflexible and dogmatic, but we all know there are ways to weasel around every rule without necessarily breaking it. There are also many situations where the strict application of the law can result in consequences that are clearly counter to the intent of the law. Principles address the spirit of the law and drive us toward certain behaviors. However, principles can also be vague, lead to ambiguity and be difficult to enforce.

An example of a letter of the law, rule-based approach can be found in ERISA §406(a)(1)(c). This section prohibits plan assets from being used to pay ***any*** party for ***anything*** including, but not limited to, investment expenses, administrative expenses, or record keeping. There's certainly no ambiguity here, and the writers of ERISA waited to include an exception to this rule in an entirely different section.

This "exception to the rule" technique serves as an indication of how serious the authors were about safeguarding the retirement plan assets of participants. We find the following exemption in ERISA §408(b)(2) in order to provide services to the plan. It states that all three of the following criteria must be satisfied in order to qualify for the exemption: 1) The services must be necessary for the operation of the plan; 2) The services must be furnished under a contract or arrangement which is reasonable and; 3) No more than reasonable compensation is paid for the service.

Unfortunately, a philosopher was not among the men and women who wrote ERISA because they incorporated an ambiguous philosophical term with the word "reasonable." While the absolute, unambiguous nature of 406(a)(1)(c) serves as a valuable concrete rule, the ambiguity of the word "reasonable" in 408(b)(2) is far from concrete. This word has probably cost retirement plan participants billions of dollars since the first 401(k) was funded nearly 40 years ago.

An example of a spirit of the law, principle-based approach can be found in ERISA § 404(a)(1)(B). Often labeled the "prudent expert rule," this section mandates that plan sponsors discharge their duties "with the care, skill, prudence and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims." Prudence is most often the focus of this clause, but prudence, skill, and diligence are all components of the ethical principle of due care.

The principle of due care is an act or a course of action that is required of one by position, social custom, law, or religion, and often as a moral obligation. While the notion of care is straightforward, the concept of “due” often is not. The word “due” is the root of the word “duty” and it implies an obligation to act. The relationship we have with our physician is a common example of the principle of due care.

If someone visits his physician because his elbow is sore, the physician doesn’t just examine his elbow. The physician conducts an assessment of his overall condition. It is the physician’s obligation to look at the big picture, not merely to treat the elbow. Similarly, it is the fiduciary’s obligation to look at a participant’s retirement health, and not merely at any given characteristic of their 401(k) plan.

Chapter 3 Demographics

Fiduciaries are instructed to choose their target date funds on the basis of workforce demographics. So say the Department of Labor (DOL) and prominent ERISA attorneys like Fred Reish and Marcia Wagner. Frequently cited demographics include salary, savings and age. In principle, demographics are intended to lead the fiduciary to an appropriate glide path: the establishment of appropriate risk for young people and how that risk should adjust through time as an employee ages.

Risk tolerance is the most important demographic cited by authorities, but this is an attitude that can only be inferred. This chapter provides insight for this inference.

Focusing on the Most Important Demographic

This is a complex mandate that can be substantially simplified, following Einstein's advice to "Make everything as simple as possible, but no simpler." Simplification begins with noise reduction. Our sole focus should be on those who default their investment decisions, since most assets in TDFs are there by default. **What is the distinctly decisive demographic that characterizes defaulted participants? It's a lack of financial sophistication.** This can be confirmed with a financial literacy quiz, but the mere fact that participants can't make an investment decision is strong evidence. This doesn't make them dumb. Will Rogers said, "Everyone is stupid, but about different things." Most individuals outside the financial profession know little about investing. Educating them is not the answer. An appropriate glide path is.

The Appropriate Risk Decision for the Unsophisticated

But what is appropriate for the naïve? If 2008 taught us anything it's that TDF participants believe they are safe, especially as they near retirement. Participants in 2010 funds had no idea they could lose 25% of their savings, and they will never understand what happened. In other words, the risk tolerance of the unsophisticated is very low. **When you're walking in the dark every stumble is scary**. The naïve need to be protected, especially as they near the end of their careers. This argues for conservatism near the target date – the more, the better. A 2012 survey of investment consultants by the Center for Due Diligence reveals a very low risk tolerance on behalf of those near retirement.

Choosing a Target Date Fund

How safe should participants be? Therein lies the big disagreement among TDF providers. Equity allocations near the target date range from zero to 75%, with the balance of assets typically in long-term bonds which are, of course, risky too. The decisive demographic argues for the low end of this range, invested entirely in safe T-bills and short-term

TIPS at the target date. It's the ultimate in safety. You can judge whether or not this is too safe, but please be aware that this safety is intended to be in place only for the last year of employment, after which most withdraw their accounts. It is not intended to be an asset allocation in retirement. The view is that you can't be too safe when it comes to protecting the vulnerable, the unsophisticated.

The most important fiduciary decision is deciding on the glide path. Once that is in place, the criteria for selecting a specific manager can be established, as described in Chapter 5.

Legal Guidance

Perhaps more than any other regulatory agency, the Department of Labor (DOL) lives in the world of demographics. One only need look at the index of topics on the DOL website: employment, personnel, grievances, wages, and so on and so on. The DOL lives in the world of the Bureau of Labor Statistics: numbers and numbers. So, when you browse the DOL's article archives, you see lots of demographic tables. The DOL understands slicing and dicing, but not necessarily drawing conclusions.

ERISA cases have been consistent in stating that investment objectives have to be specific to the individual investor. How can the DOL possibly apply that to ALL the participants in a large 401(k)? Not possible. So take an average. A good mathematician (if we can find one) will tell us that averages are skewed by the high and low ends. Is it possible to establish glide paths that will cover all your participants? No.

Is it possible to customize glide paths that fit every possible set of individual facts and circumstances with any precision? Of course not.

Ethical Perspective

The discussion above has a section entitled "The Appropriate Risk Decision for the Unsophisticated." Synonyms for the word "unsophisticated" include inexperienced, naïve and childlike. Parents must make many decisions for children because children aren't sophisticated enough to make them for themselves. All of us are unsophisticated about many things so we often trust experts; again, our physician is the classic example. The Doctor-Patient relationship, just like the Parent-Child relationship, is a fiduciary relationship. We trust that our physician is competent and acting in our best interests. We are vulnerable to the decisions they make and the risks they might take in our treatment. Ideally, we are protected by the extensive mandatory training required to become a physician and by the American Medical Association Code of Ethics.

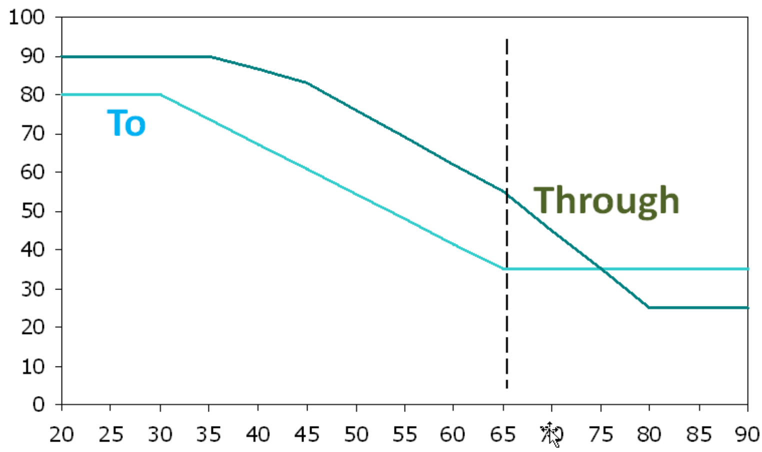
The plan sponsor – plan participant relationship is no different legally or ethically. Studies have shown that a majority of plan participants are unsophisticated when it comes to investing. Retirement plan fiduciaries would likely argue that they have no fiduciary training and that they are not fiduciary experts. Unfortunately, ERISA holds them to the status of a prudent expert and obligates them to fulfill their fiduciary responsibilities. While this situation might seem absurd, there is a caveat to this obligation that states: "Unless they possess the necessary expertise to evaluate such factors, fiduciaries would need to obtain the advice of a qualified, independent expert." Reg. § 2509.95-1(c)(6)

Chapter 4
To or Through

Most target date fund due diligence begins with a distinction between "To" and "Through." The DOL recommends that fiduciaries make and document this decision, but it is misguided advice. The words "To" and "Through" were coined at the June, 2009 joint SEC and DOL hearings on target date funds which examined the devastating losses of 2010 funds in 2008. The testifying fund companies explained that they take substantial risk at the target date because their glide paths serve "Through" the target date to death. This is in contrast to funds called "To" funds that end at the target date. The clear implication is that "To" funds are far less risky at the target date than "Through" funds, but this is not true because the industry has elected to define "To" in a bizarre way, much like President Clinton defined the word "Is." "To" is being defined as a flat equity allocation beyond the target date. **This is unfortunate because the very essence of "To" is the non-existence of "beyond."**

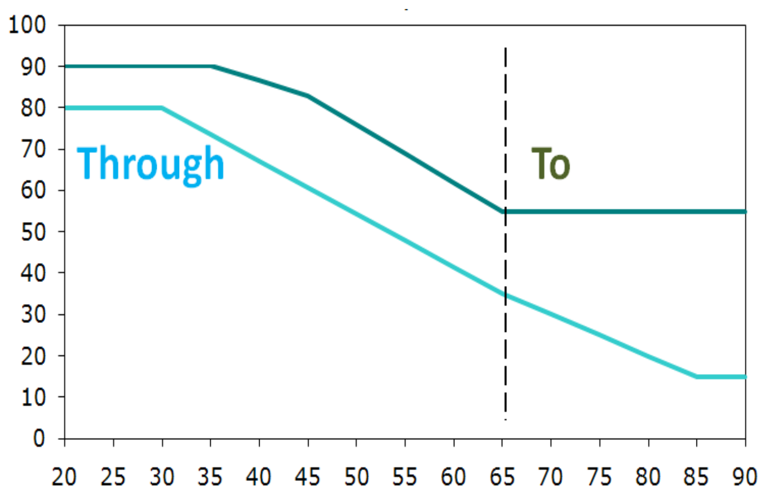
The words "To" and "Through" were used at the target date fund hearings to mean:

- **Through**: Target date is a speed bump in the highway of life.
- **To:** Target date is the end of the investment mission. Accumulation only.



Accordingly, the common belief is that "To" funds hold less equity at the target date because they end there, as shown in the graph on the right.

But "To" funds are being defined as any fund with a flat equity allocation beyond the target date. Why does allocation beyond the target date matter if the intention is to

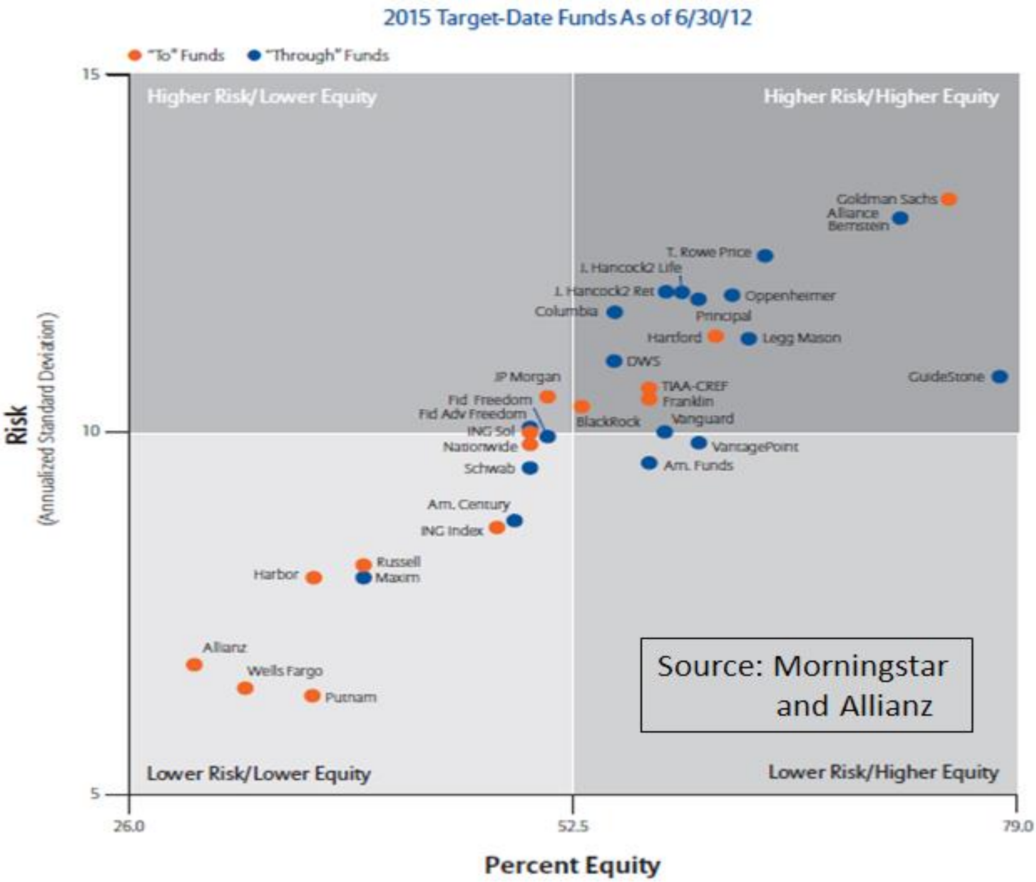


end at that date? **<u>The trick is appearing to end without really ending.</u>** The pretext is that any fund that reaches its lowest equity allocation at target date is a "To" fund because changes in the glide path have ended, even though the fund continues on. Fund companies want to keep assets as long as possible, despite emerging investor interest in "To" funds. Fiduciaries believe a "To" fund is safer and more prudent, and it should be. "To" should be safer than "Through", but it might not be, as shown in the graph above.

A Distinction Without a Difference

The bottom line is that "To" versus "Through" is a distinction without a difference because:

- All "**<u>To</u>**" funds want to keep the assets beyond the target date. They are only pretending to end. They are not accumulation only.
- All funds, both "To" and "**<u>Through</u>**," effectively end at the target date because most participants withdraw their accounts when they retire.



The reality is that the equity allocations at target date of most "To" funds are just as high as "Through" funds. A fund with a 100% ending equity allocation at target date is a "To" fund under the flat path definition as long as it maintains that exposure beyond target date. Also, all static mix balanced funds are "To" funds using this peculiar flat path definition.

"To-Through" is a distinction without a difference as shown in the Exhibit on the right, where "To" funds are shown in red and "Through" funds are shown in blue. For example, you can see that the Goldman Sachs "To" Fund is the riskiest while the Maxim "Through" Fund is among the safest.

Make it Stop

Fiduciaries should not allow this gimmickry to stand. "To" should not mean "Flat Path." "End" should not mean "Continue." No cigars for "Is." Fiduciaries should take heed of equity allocations at the target date, and be aware that real "To" funds do exist and the acid test is that there is no risk in the "beyond." Real "To" funds actually end at the target date and are truly designed to be accumulation only. Real "To" fund glide paths land safely in prudent investments like TIPS and Treasuries, and it doesn't matter what happens beyond the target date because the presumption and hope is that beneficiaries will move assets to distribution-type vehicles like annuities and managed payout funds, as they should.

Legal Guidance

Fiduciaries have a legal obligation to attempt to mitigate risk in their participants' portfolios. The DOL has stated that the selection of fund vehicles and options for participants requires the same level of analysis as an investment in any other ERISA plan. "Plan fiduciaries have an ongoing duty to consider the suitability of a designated [401(k)] investment vehicle which encompasses the continued determination that the vehicle remains a prudent investment option." There are a lot of considerations, like performance, focus on low expense, diversification, and so on.

In other words, there is much more to prudent selection than "To" versus "Through", even if this distinction actually mattered.

Ethical Perspective

We noted earlier that the principle of due care obligates a physician to look at a patient's overall health. Inherent in this principle is the notion of due diligence. Imagine if a physician prescribed a new drug after only a cursory review of its marketing material. Without a thorough understanding of this drug, the physician's decision could actually harm the health of a patient.

Since ERISA's concrete rules can sometimes be at odds with its ambiguous principles, the Golden Rule is a valuable rule of thumb to evaluate one's actions under ERISA. When it comes to determining a specific course of action or one's fiduciary responsibility in a situation, ask yourself "What would I want my plan sponsor to do for me in this case?" At a minimum you would likely want your plan sponsor to conduct the appropriate due diligence and weigh the pros and cons in order to make an informed decision that would enhance your opportunity to achieve a secure retirement income.

Chapter 5 Establishing Criteria

As discussed in Chapter 3 on Demographics, the primary fiduciary objective for TDFs should be protection, because the risk tolerance demographic of defaulted participants is very low. Participants in TDFs think they are safe. Don't lose participant savings. The secondary objective is to earn as much as possible, without losing participant savings. In this chapter we establish criteria for achieving these objectives and, therefore, for choosing a specific TDF.

The benefits of target date funds are diversification and risk control (professional management), preferably at a reasonable cost, all of which a participant is unlikely to achieve on his or her own. The ideal TDF provides maximum diversification, especially at the longer dates when there is more risk. As the target date nears, rigorous risk controls guard against losses. These benefits should be provided at the lowest cost possible and should employ a glide path design that is comprehensive and reliable. Let's examine each of these criteria individually.

Diversification

The world market portfolio is the ultimate in risky asset diversification, encompassing the following:

- Global stocks
- Global bonds
- Global real estate
- Global commodities
- Global natural resources
- Other diversifying assets

This portfolio should be used for younger participants, at longer dates. Then as the target date nears, the brakes need to be applied using rigorous risk controls.

Risk Control

Safety at the target date is paramount. There are compelling reasons for no risk at the target date. By "zero risk" we mean no stocks and no bonds, just short term TIPS and T-bills.

Zero Risk at the Target Date

1. There is no fiduciary upside to taking risk at the target date. Only downside. The next 2008 will bring class action lawsuits.

2. There is a "risk zone" spanning the 5 years preceding and following retirement during which lifestyles are at stake. Account balances are at their highest and a participant's ability to work longer and/or save more is limited. You only get to do this once; no do-overs.

3. Most participants withdraw their accounts at the target date, so "target death" (i.e., "Through") funds are absurd, and built for profit.

4. Save and protect. The best individual course of action is to save enough and avoid capital losses. Employers should educate employees about the importance of saving, and report on saving adequacy.

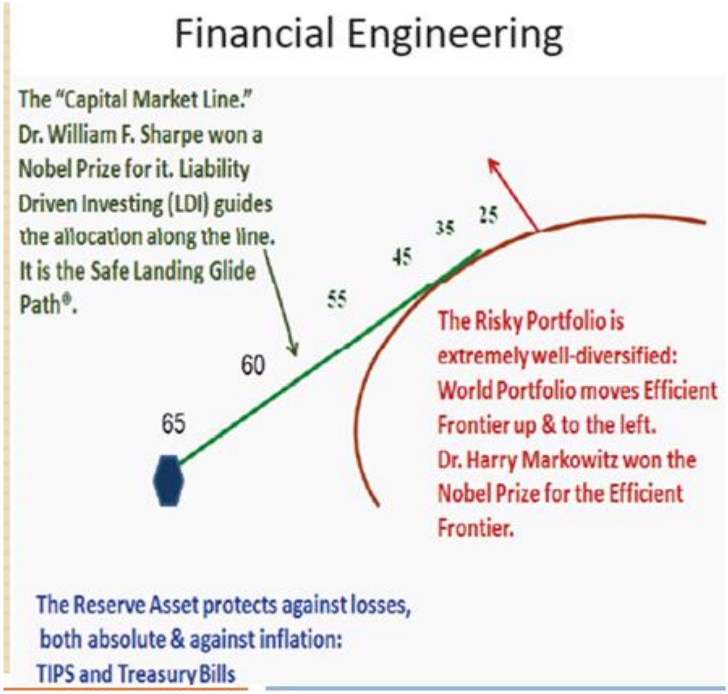
5. Prior to the Pension Protection Act of 2006, default investments were cash. Has the Act changed the risk appetite of those nearing retirement? Surveys say no.

6. Ignoring the past (especially 2008) and hoping it's different the next time is not an option, and it's certainly not an enlightened view of risk management.

Fees

TDF fees currently average around 100 basis points (one percent). The ideal TDF should be provided for less than 50 basis points. This low fee is not hypothetical. It is well within the realm of possibility.

Sound Design



The patented Safe Landing Glide Path® (SLGP) sets a standard for TDF design. The SLGP integrates the tenets of Modern Portfolio Theory with the disciplines of risk management and liability-driven investing. When the target date is distant, a world portfolio (the ‘Risky Asset”) is used to optimize return per unit of risk, encompassing a globally defined mix of the major asset classes, including stocks, bonds, real estate and commodities. As the target date nears, account balances are increasingly placed in a safe “Reserve Asset” that is comprised of short term, inflation-indexed Treasury securities (TIPS) and 90-day Treasury bills. The SLGP estimates the worst-case loss on the Risky Asset from today’s date to the target date, and allocates to Reserves to compensate for that loss. If a worst-case loss of Risky assets actually occurs, the fairly safe return on Reserves should make up for that loss. As a result, the SLGP is almost entirely in Reserves at the target date, an essential feature that is ignored in most target date funds. Put another way, substantial losses on Risky assets can happen very quickly, so those nearing retirement are in jeopardy unless they hold very little in Risky assets. Stuff happens.

Legal Guidance

As pointed out above, the most obvious problem with most TDF providers is that their fees are too high. 1 percent should not be an acceptable fee for a relatively passive investment option. So, let’s focus on fees as an example of plan sponsor lack of awareness and exposure to litigation. The next round of lawsuits could very well involve TDF selection.

Excessive fees are on the DOL hit parade, yet many plan sponsors simply aren't aware. It is a fundamental education problem. We already pointed out that too many plan sponsors are not even aware of their fiduciary responsibility, so they stumble along being willing prey for every advertisement, every sales pitch. The small plans are not even candidates for professional investment consulting advice. There's no money in it for the consultant.

In the past, ground-breaking ERISA lawsuits made headlines read by pension plans, unions and institutions. To date (March, 2014) there have been some really ground-breaking lawsuits on the fee issue, but the "little guy" plan doesn't know about them, and doesn't know its legal liability exposure.

Our real challenge as "educators" is to get this information out to everyone. Financial advisors should give back some of their time *pro bono* to help educate those who need it most. I'm betting that's unlikely.

Let's look at 408(b)(2) required fee disclosures and a couple of fee cases:

408 (b)(2) is a new rule that impacts 401(k) accounts in terms of the disclosure that must be provided to investors. Managers must disclose direct and indirect compensation, including soft dollars. Also sponsors must provide sufficient information to participants: returns, benchmarks, strategies and risks, and portfolio turnover. The penalty is breach of fiduciary duty, and personal liability. The issue is compensation "broadly construed". Advice: Err on the side of caution: is it compensation? If you don't know, better disclose it.

Tibbie v. Edison

Court ruled that the investment committee violated ERISA's duty of Prudence by "not properly investigating the differences between selecting Retail & Institutional share classes."

Tussey v. ABE Inc.

"...the Court finds that the Plan overpaid for Fidelity Trusts record-keeping and administrative services ... Accordingly, the Court finds that the Plan suffered losses of $13.4 million as a result of ABE's failure to monitor record-keeping costs

[...] All ABE defendants are held jointly and severally liable for this amount."

A court held that a fiduciary had an affirmative duty to inform participants about circumstances that could jeopardize benefits.

There are hundreds of cases against plan sponsors for allowing excessive fees, not monitoring performance, using proprietary funds from a fund company, etc.

No case is too small. Fiduciary duties are the same whether the plan has $275,000 or $8.5 billion.

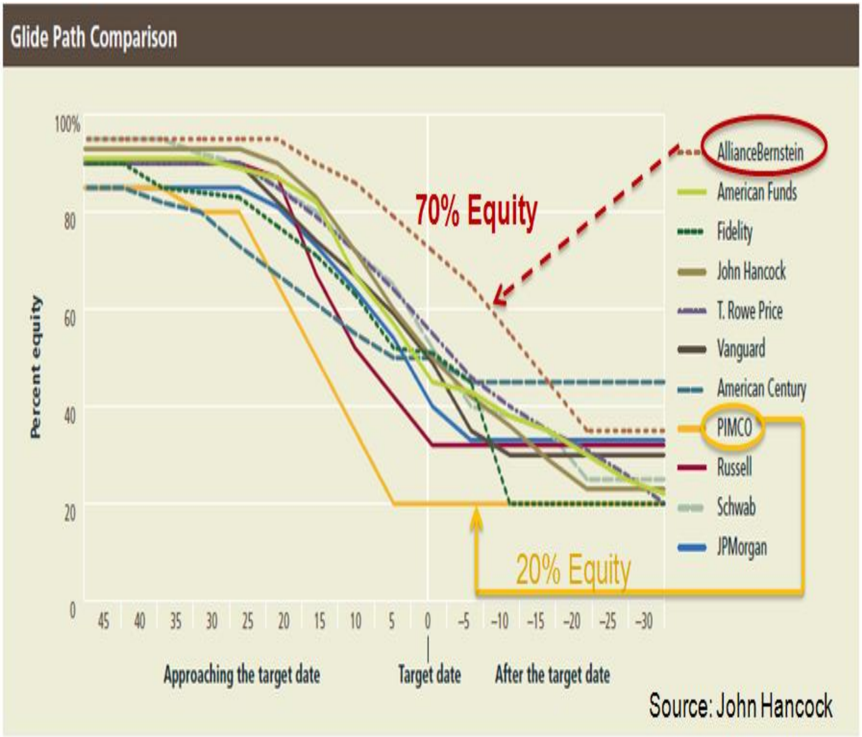
Ethical Perspective

A prudent course of action, just like an ethical decision, is sometimes difficult to determine. Many philosophers have applied the *veil of ignorance* to these situations. Here's how it works. Imagine your intellect separate from all of your personal characteristics – your gender, age, religion, socio-economic status, whether you are a plan sponsor or a plan participant, etc. As such your intellect would have no bias or prejudice.

Now imagine your intellect buying a widget. What criteria would a reasonable person consider in buying a widget – obviously one key consideration is price. What if there were two identical widgets; identical in every characteristic except for price. Can you imagine a situation where it would be rational to pay more for a widget when you could pay less for the exact same widget? Unless someone can come up with a rationale where it made sense to pay more instead of less, then buying the more expensive widget is imprudent.

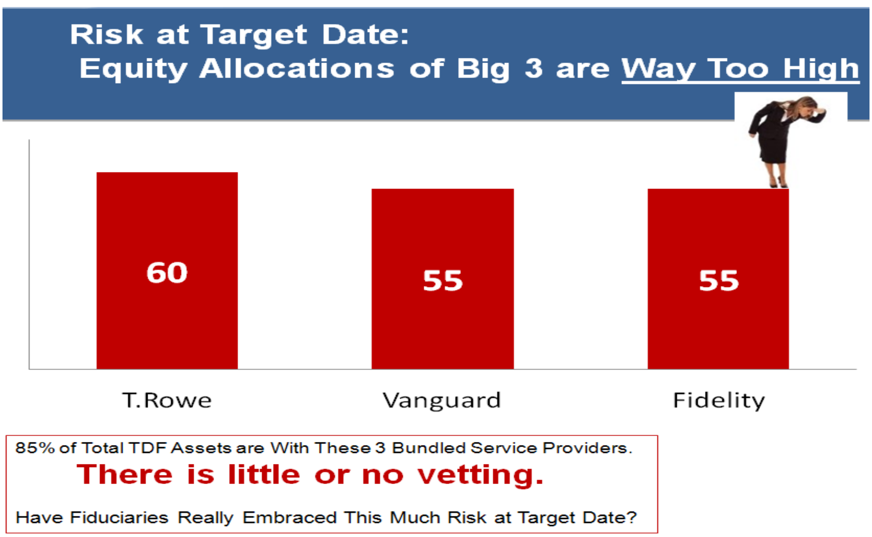
Chapter 6 Current Practices

Currently, a "Glide Path Debate" is raging on, focused on equity allocations near the target date. As shown in the following graph, there is consensus among TDF providers at long dates, far from the target date – the allocations cluster. However, there is a wide range of exposures near the target date.



The Problems Just Won't Go Away Unless Fiduciaries Act

As a practical matter, this debate is moot because most TDF assets are invested with the Big 3, with ending equity allocations around 55%. As is characteristic of many investment products, fund companies are calling the shots in target date fund investments. Consequently, little has changed to remedy the 2008 debacle. The Big 3 – T. Rowe Price, Fidelity and Vanguard – continue to manage the majority of TDFs, primarily because they are the largest



bundled service providers. The problem isn't that the biggest are used most; it's that fiduciaries are not researching and evaluating the myriad TDFs that are available to plan participants. They are not even looking at alternatives. Choosing one of the Big 3 might be alright if competing TDFs were all inferior, but they are not. Most important, these Big 3 maintain the same equity exposure today at the target date as they had in the 2008 fiasco, setting the stage for a repeat calamity, this time much more devastating.

The typical target date fund remains invested 55% in equities at the target date, the same as it was in 2008. The objectives also remain the same -- to replace pay and manage longevity risk -- but you won't find these stated in prospectuses or factsheets – just in sales pitches. Importantly, no "glide path" can reasonably be expected to replace pay or manage longevity risk, so there is a high risk of failure. **The Sad Comedy of Target Date Funds** portrays the problem in a short video. The right course of action for achieving these objectives is to save enough.

Ignoring the past (especially 2008) and hoping it will be different the next time is not an option, and it's certainly not an enlightened view of risk management. Fund companies argue that 2008 losses have subsequently been recovered, so no harm no foul, but the reality is that most participants in 2010 funds have withdrawn their savings so they did not partake in the recovery.

Fiduciaries are Relying on Mistaken Beliefs

Fiduciaries sign on for this mistake because they believe that they are protected from litigation by two safe harbors in their selection of target date funds:

1. Properly structured TDFs are Qualified Default Investment Alternatives (QDIAs) under the Pension Protection Act of 2006. Form over substance.
2. There is safety in numbers, so choosing one of the most popular TDF providers is prudent. You can't go wrong with Fidelity, T. Rowe Price and Vanguard. Or can you? Is common practice necessarily prudent?

There is more to selecting TDFs than these two simple rules. Reliance on these trifling shields can lead to breaches of fiduciary duty that will bring lawsuits (loss-suits) when we experience the next 2008. Most TDFs are ticking time bombs because they are too risky at the target date. These bombs will explode in the faces of fiduciaries as well as their unfortunate employees.

Fiduciaries are exposed to lawsuits because they have the duty of care, so they are obligated to actually vet their TDF selections and to establish objectives that are truly in the best interests of participants. Fiduciaries are duty-bound to seek solutions rather than settling for high-risk products that are oblivious to history.

Legal Guidance

The DOL announced it has a "Hit List" to pursue the following national enforcement 401(k) issues.

- Late or missing employee contributions.
- Administrative or documentation mishaps.
- Overweighting in employer stock—looking to prevent Enron-type fraud situations.
- Overpayment of fees to funds and service providers, and lack of disclosure of such fees.
- Abuses or negligence in hiring service providers.
- The failure to allocate assets as a result of complicated financial transactions.
- Imprudent investment decisions.
- Other abuses or negligence in handling contributions.

The common thread running through these actions is that companies are being found to have no one minding the store regarding 401(k) accounts. There must be an appropriate amount of due diligence applied to suitable investments, service provider fees, value of company stock, and investment communication to employees about the financial capacity of the company. It started with Enron and won't stop until mom and pop companies are also corrected.

So, what is an employer to do?

<u>10 TIPS for employers:</u>

1. Decide which 401(k) plan type is right for you
2. Review providers and purchase your plan: BIGGEST IS NOT BEST. DO YOUR RESEARCH!
3. Select plan features that best fit your needs
4. Rollout your 401(k) plan to your employees
5. Make your contributions automatic each payroll
6. Take advantage of annual tax credits and deductions for your business
7. Once your 401(k) plan is up and running, review your own account once or twice a year to ensure your investment direction still aligns with your goals

8. Keep your employees’ fees less than one percent

9. Choose a plan design that fits your business’ specific needs now, and a provider that has the services and options that can grow as your company evolves

10. Seriously consider a provider that manages your company’s investment roster

Ethical Perspective

An earlier heading in this chapter summarizes the ethical perspective here, *The Problems Just Won’t Go Away Unless Fiduciaries Act.* Right or wrong is often perceived as shalt not’s or things that we are not supposed to do. The West Point Honor Code includes three shalt not’s: “A Cadet shall not lie, cheat or steal.” From the earliest age we are all taught what not to do, and ethically these are known as negative obligations.

But the principle of due care focuses on the shalt, which is much more challenging. We control our own actions and can decide for ourselves not to lie, cheat or steal. But what if we are obligated to act based on the actions of another?

Consider the second clause in the West Point Honor Code: “or tolerate those who do.” This clause is an affirmative obligation. At West Point, a common ethical question is, what would you do if you discovered that your best friend cheated on an exam. If you do nothing, you have violated the Honor Code and could potentially be expelled from the Academy. However, most of us would find it very difficult to take action that could result in their best friend being kicked out of West Point.

Affirmative ethical obligations are not a matter of what one can or cannot do; it’s a matter of what one ought to do. ERISA attorney Fred Reish emphasized this when he said, “Fiduciaries are not sued for what they do, instead they are sued for what they do not do.”

Chapter 7 Benchmarks

Fiduciaries are obligated to monitor and evaluate the performance of their TDFs, but relative to what? Much debate and controversy surround the benchmarking of target date funds (TDFs). The challenge revolves around the fact that the asset allocation and, therefore, risk of TDFs changes through time. But, if fiduciaries will take a step back to look at the big picture, they will recognize only two choices: Procedural Prudence or Substantive Prudence. The fiduciary can use a benchmark that captures common practice, which is a Procedural Prudence benchmark. Procedural Prudence is satisfied when a fiduciary acts as others in a similar capacity act, following commonly accepted processes: follow the herd. The S&P and Morningstar Target Date Indexes are good benchmarks for Procedural Prudence because they are composites of all TDF mutual funds – they are consensus indexes. By contrast, a benchmark of Substantive Prudence reflects best practices, doing what is right for the beneficiaries, regardless of common practices. This may sound like a high and mighty benchmark, but it's not. Its derivation ties directly to something quite simple: what are the appropriate objectives for a TDF.

Common practice objectives for TDFs are to replace pay and manage longevity risk. These are not objectives at all – they are mere hopes, and, even worse, they are hypes. An objective without a reasonable course of action is a hope. One-size-fits-all-set-it-and-forget-it TDFs cannot achieve these objectives. Saving enough is the right course of action for these common practice objectives.

The Substantive Prudence Benchmark

By contrast, reasonable objectives that represent best practices are capital preservation (don't lose money) and earn as much as you can without losing money. These Substantive Prudence objectives can be met by following the patented Safe Landing Glide Path® described in Chapter 5. This glide path is the other choice for benchmarking TDFs. It is provided by the BrightScope On Target Indexes® (OTI).

Legal Guidance

Procedural prudence benchmarks fail in the courts. Herd mentality is inadequate (The Lemming analogy). The better choice is substantive prudence because it is in line with the core principles of ERISA which direct that all activity must be conducted in the best interests of participants and beneficiaries. Mechanically, the only "safe" prudent process would be to attach individual benchmarks to each participant, taking into account all the relevant facts and circumstances of each individual's financial and personal circumstances. Of course, this is not practical in big plans.

The 1974 Conference Report on ERISA lists three ways a fiduciary can satisfy his responsibilities when investment management is allocated or delegated: a formal periodic review, day-to-day contact and evaluation or "other appropriate ways." While ERISA clearly requires a monitor and evaluation procedure, the method is not spelled out. It remains a case-by-case situation.

It is now established ERISA law that fiduciaries are required to perform regular performance reporting, monitoring and evaluating of plan assets. Cases that impose this strict standard include:

- Whitfield v. Cohen (11 EBC 1739) Trustee liable because he did not monitor the progress of investment manager.
- Martin v. Tower A detailed evaluation process as an integral part of the holding.
- Jones v. O'Higgins (11 EBC 1660) Performance monitoring a fiduciary duty.
- Dardaganis v. Grace Capital [11 EBC 2081 (CA 2d 1989)] Performance monitoring a fiduciary duty.

The law is clear, but the process to satisfy it is not. No advice here, other than establish a monitoring (see Benchmarking above) process and make it defensible. We're open to suggestions.

Ethical Perspective

The distinction between substantive prudence and procedural prudence is similar to the distinction between the principle-based ethical theories and rule-based ethical theories.

Substantive prudence is based on principles and points us toward retirement income security. Procedural prudence is based on rules and provides specific directions on how to achieve retirement income security. We have noted the advantages and disadvantages of both the rules-based approach and the principle-based approach. However, ERISA offers no rules specific to TDF benchmarks; therefore, we necessarily must decide based on the principles.

A fiduciary must exercise loyalty, prudence and due care in choosing a TDF as well as the appropriate benchmark.

In making these choices, the following three questions might be helpful:

1) Am I choosing this fund in the sole interest of my participants?

2) Have I prudently sought the best available choice for my participants?

3) Have I exercised due care by ensuring this choice will provide my participants with the greatest opportunity to achieve retirement income security?

Chapter 8

Statement of Investment Policy

Statement of Investment Policy

Objectives and Risk

We, the fiduciaries to the retirement plan, regard risk as the possibility of failing to achieve objectives. Accordingly, the purpose of this statement is to document our goals and how we plan to achieve them. The objectives and risks of the selected target date fund are:

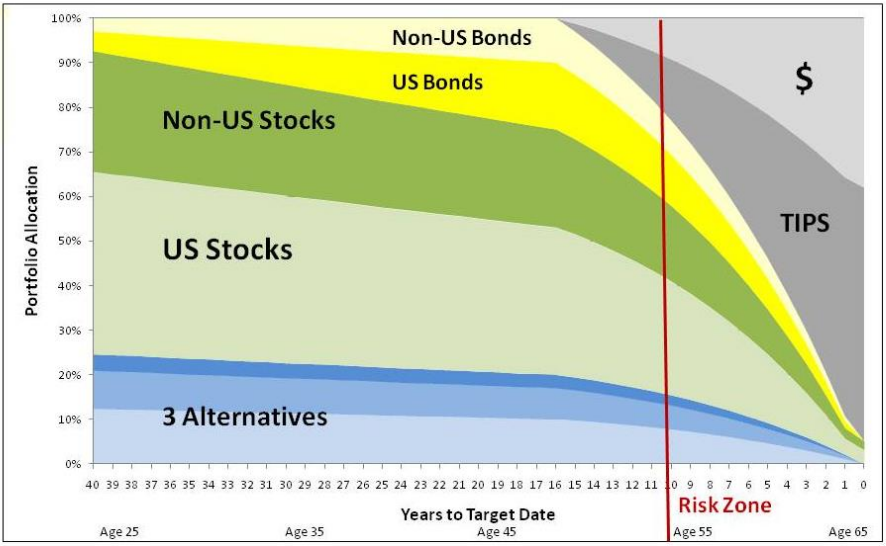
1. Deliver at least accumulated contributions plus inflation at the target date. Strive to achieve this objective with high conviction (i.e., low risk).
2. Grow assets as much as possible without jeopardizing the primary preservation objective. We would like a high probability of achieving this objective when the horizon (term to target date) is long, but will sacrifice growth for safety as the target date nears.

Policies

The policies for achieving these objectives employ a 2-asset growth-preservation separation principle. In the early years, a very broadly diversified growth portfolio serves to increase wealth, but then about 15 years from target date the fund employs Liability-Driven Investing (LDI) principles to defend, moving monies aside into a "Reserve" lock-box of TIPS and Treasuries.

Glide Path

The glide path controls risk through time and is designed to emphasize growth in the early years and then move to defend fairly quickly as the target date nears. The following graph and table describe this path. As shown in the graph, there is a "Risk Zone" that starts 10 years prior to the target date during which account balances are at their highest and lifestyles are at stake. The SEC and DOL understand this. The focus of their hearings and proposals has always been on risk near the target date. There is no fiduciary upside to taking risk during this critical period.



Selected Target Date Fund Asset Allocations

Years to Target	Equity	Alternatives	Bonds	TIPS and T-bills
0	5	0	0	95
10	42	15	20	23
20	57	21	22	0
30	63	23	14	0
40	68	25	7	0

Architecture and Expenses

Our target date fund is entirely open architecture, meaning no proprietary funds are employed. Furthermore, most of the underlying funds are broadly diversified and passive, which lowers costs. The high-water mark on underlying fund expenses occurs at about 15 years to target and is less than 30 basis points. When management fees, custody, administration and other associated costs are added in, the all-in costs are generally less than 50 basis points.

Experience and Credentials of the Fund Provider

John Doe is the designer and developer of the selected target date fund. John has 35 years of experience in investment program design and investment policy setting. He earned an MS in Applied Mathematics with Honors from the University of Illinois and an MBA in Finance from the University of Chicago.

Performance Expectations and Reporting

In normal (positive) stock market environments, we expect near-dated funds to lag in performance relative to the industry, as represented by the Morningstar Target Date Index for To Funds. This is the opportunity cost of emphasizing safety near the target date. Regarding all funds the usual risk-reward trade-offs will apply, so we expect that the reward-to-risk ratios of the funds will dominate those of the industry at all target dates. We also expect that over a full market cycle the longer-dated funds will dominate the industry on both a return basis and a reward-to-risk basis because of the broader diversification employed by the funds.

Performance will be reported quarterly to fund participants. The fund is benchmarked against the BrightScope On-Target Indexes® (OTI).

Legal Guidance

The primary principle to observe in investing other people's money is to establish investment policy. The DOL virtually mandates an investment policy for achieving objectives. The investment policy statement (IPS) is the keystone of compliance with fiduciary responsibilities. An investment policy without supporting written documentation is a penguin—it will not fly. The only way that a prudent fiduciary can meet his obligations is to clearly set down a well-thought-out investment policy statement for achieving appropriate objectives consistent with the fund's documents and instruments. Only then will the fiduciary be able to defend all future actions relating to the investment of those funds, assuming they are consistent with the policy.

The minimum requirements for a statement of investment policy include:

- A statement of objectives
- The method for selection, monitoring, evaluating, retaining, and firing investment managers
- Policies for achieving objectives, for supervising investment performance, and for making this information available to participants and beneficiaries

Managers have to consider the investment policy statement, which includes guidelines for investing, appropriate courses of action, and portfolio monitoring. The process clearly implies the usage of an investment management consultant.

Unfortunately, I estimate that 80 percent of smaller plans (less than $3 million) do not have written investment objectives and policies.

Ethical Perspective

In Chapter 3 we addressed the vulnerability of the unsophisticated plan participant, because most assets in TDFs are there by default. TDF assets belong to the unsophisticated. Once again the physician analogy is helpful here. The most fundamental ethical principles for a physician are found in the Hippocratic Oath: Make a habit of two things: to help, or at least, do no harm.

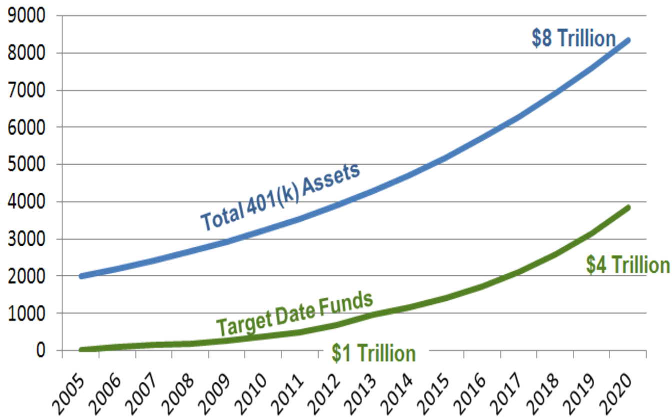
While this obligation is just a brief few words, the underlying ethical principles are significant and relate directly to the fiduciary responsibility of plan sponsors. The two principles are beneficence and non-maleficence. The principle of beneficence is an affirmative obligation to do good and is summarized as acting in ways that promote the well-being of others. The principle of non-maleficence is a negative obligation to “do no harm,” to act in ways that do not cause harm to others.

A plan sponsor could apply these principles to any ethical decision if they act in ways that enhance a participant’s opportunity for a secure retirement income; and do not act in ways that diminish a participant’s opportunity for a secure retirement income.

We might consider enhancing a participant's opportunity for a secure retirement income as investment growth. And not diminishing a participant's opportunity for a secure retirement income as, at least, maintaining the buying power of a participant's assets.

Chapter 9
The Future

Looking ahead, target date funds are projected to quadruple in the next 5-6 years, reaching $4 trillion, which will equal about one-half of all 401(k) assets. In other words, TDFs will become increasingly important.



Source: Target Date Solutions

Sometime in the future there will be a market correction of the magnitude of a 2008 or even a 1929. Unless risk controls are tightened, especially near the target date, fiduciaries will be sued as a result of losses. It remains to be seen whether the litigation will impact fund companies or fiduciaries, or both. Mutual fund companies do not stand as fiduciaries relative to the pension plans that invest in them.

TDFs will be quite different after this cleansing. It will take "the stick" to stir things up because "the carrot" is not working.

Legal Guidance

Regulators are reactive. They adhere to the age-old premise "follow the money." The target hit list for the DOL will always focus on those areas that are most used, have the highest inflows (possibly outflows as well), and are getting the most publicity and attention. They are the "low hanging fruit." Since a regulator's annual budget is influenced by its success in prosecuting, fining or otherwise "catching" a perpetuator of risk to participants and their beneficiaries, any regulator will follow the easy-to-catch.

Similarly, client advocates (swarms of class action lawyers) will advocate for the higher numbers. Remember contingency fees. Watch for advertisements and articles warning of some practice or other that could generate litigation.

The poor sap, the financially unsophisticated participant, will take some of this media-driven advice to heart and maybe remember it when his or her 401(k) is inadequately funded or, even worse, unable to withstand the next 2008.

Where does that place TDFs? Increased use, popularity, sales touting, asset flow, media hype, and the FIRST complaint (regardless of where it originates) will open the proverbial floodgates of litigation. It really doesn't matter much whether the practices of any given TDF displays proclivities of riskiness to participants. Visibility and deep pockets will be the primary litigation attraction.

Ethical Perspective

The carrot and stick analogy brings us back to Plato's moral in the Ring of Gyges; however, Plato's most famous student points to the underlying cause of ethical and fiduciary failure. Aristotle held that one becomes ethical through habituation and that the law affects our habits.

He wrote:

"*For legislators [lawmakers] make the citizens good by forming habits in them, and this is the wish of every legislator, and those who do not effect it miss their mark, and it is in this that a good constitution differs from a bad one.*" Book II, 1103.b4

If Aristotle were to evaluate the laws, and enforcement of laws, governing fiduciaries and those who provide services to fiduciaries, he would likely conclude that our legislators have missed their mark.

Chapter 10
Call to Action

This book is written for fiduciaries who select target date funds, which means it's directed primarily to pension consultants. You alone can improve target date funds. Nothing will change unless and until you set the objectives for TDFs and seek solutions that can meet those objectives. As we witnessed in 2008, high risk near retirement is a gamble, not a solution. This gamble will pay off, until it doesn't.

"Save enough and protect it" is the simple recipe for a comfortable retirement, but it's not what is being sold by fund companies. Allowing fund companies to call the shots is not a prudent choice. Not for you, and not for the beneficiaries.

If you decide not to act, there could be a personal price to pay in the form of lawsuits. The duty of care requires that you protect the financially unsophisticated. It's like the duty to protect your young children. Fiduciary responsibilities are not fulfilled by choosing any Qualified Default Investment Alternative (QDIA), nor by choosing your bundled service provider, even if that is a popular choice. You need to try to select the best and to guard against foreseeable harm to the participants.

You can choose between acting today or risking lawsuits in the future. What is your upside in allowing the games to continue?

Chapter 11:

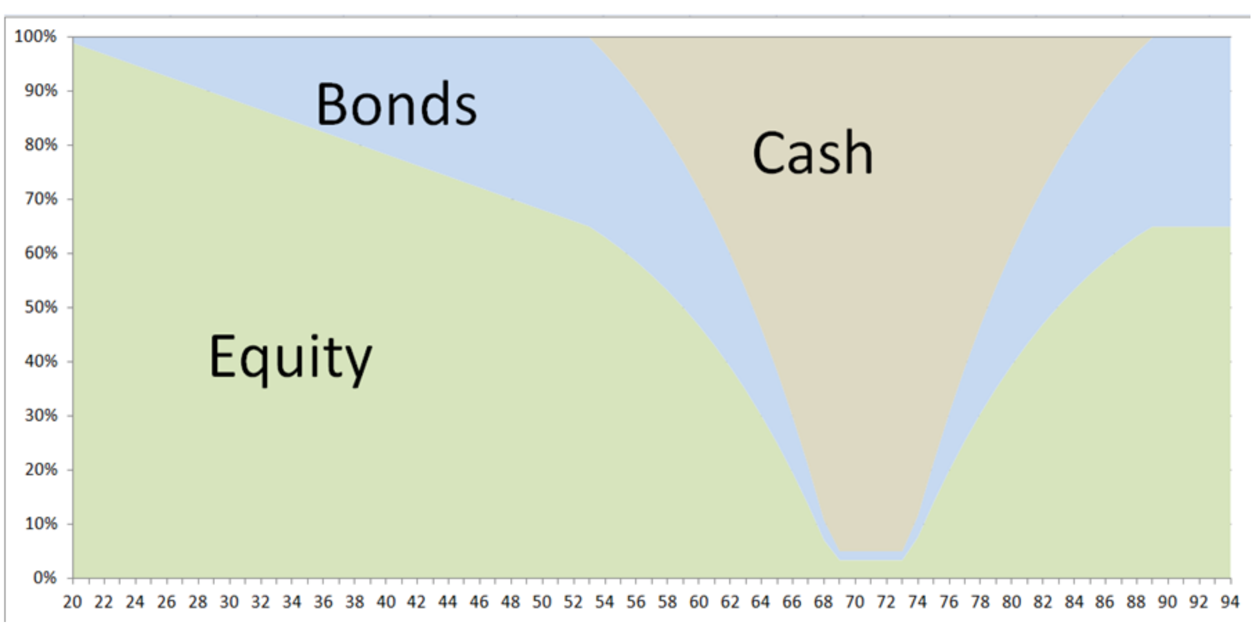
Beyond the Target Date

The number one criticism of the Safe Landing Glide Path® is that most retirees can't live on cash and TIPS. This is true, except:

- Academics argue that an all-TIPS portfolio is THE right solution for retirees, and Dimensional Fund Advisors has launched target date funds tied to this belief. The fact is that this "pockets of money" approach only works for the rich. Zero coupon TIPS are lined up to "immunize" future spending in retirement. For example, if you want to buy a $5 million yacht in 6 years, you buy a $5 million TIP maturing in 6 years.
- As we've stated throughout this book, most people withdraw their TDF accounts when they retire, so says JP Morgan. So as a practical matter there is no "beyond" for TDFs.

Nevertheless, in this chapter we address the criticism head on by extending the SLGP beyond the target date just in case some participants would like to stay invested. Here's the extension:

- The glide path stays conservative, in cash and TIPS, for 4 years past the target date because this is the Risk Red Zone during which lifestyles are at stake. "Sequence of return risk" is all about the fact that losses are most devastating when account balances are at their highest. Note that the SLGP remains a "To" fund by the definition of reaching its lowest equity allocation at the target date.
- Then beyond 4 years after target, equity allocations gradually increase following the rationale presented by Dr.Wade Pfau and Michael Kitces in their ***Reducing Retirement Risk with a Rising Equity Glidepath***



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Chapter 11: Corbis Images/F1 Online, 2011
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