NEWS REVIEW


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# Worried About Your Financial Wellness? Time to Study up on Behavioral Economics

By John Hoffmire & Ben Yound PFEEF May 2015

Have you ever wondered why you make certain decisions against your better judgment? Why is it, even when you know what is right, that choosing it is such a challenge? While moral philosophers have debated these questions for centuries, a recent entry into the debate is gaining significant attention: behavioral economics.

First identified in the 1970's, the principles of behavioral economics have come to the forefront of academic and professional research. There are many reasons for this rise, ranging from popular interest to near-universal applications, but one explanation rises above the rest: it makes sense.

A challenge often faced by non-academics with economic theory is the rationality assumption. Simply put, it assumes that in every decision, people will weigh the costs and benefits and choose the reasonable course of action to maximize benefits and minimize costs. Behavioral economics challenges this assumption by realizing that biases and perceptions sometimes cause us to choose non-ideal outcomes.

For example, a person trying to lose weight passes a box of doughnuts a co-worker brought in to share and faces a choice: take a doughnut or just walk by. The cost associated with eating the doughnut is increased calories, a feeling of defeat, and a potential workout to burn off the calories. The benefit is short-lived pleasure and a sugar rush. All things held equal, this should be an easy choice: don't eat the doughnut. But, as you likely have experienced, the situation often does not play out this way. The future cost of the doughnut is underestimated while the immediate benefit is overestimated, and the doughnut is eaten.

# Worried About Your Financial Wellness? Time to Study up on Behavioral Economics Continued…

What happened? Why weren't the costs balanced and the benefits weighed? Where is the disconnect? In short, impulse took over; an irrational choice was made. However bleak this may seem, understanding and applying behavioral economics can have real benefits as we are now able to predict when these irrational choices will occur, and plan around them.

One especially common behavioral influence is called loss aversion. Field experiments have shown that it feels more painful to lose something than it does to gain something equal in value. For instance, if I take $50 from you, it will cause more stress than the happiness you would gain if I gave you $50. The dollar amounts are the same, but the emotional responses are different.

This result can be leveraged to prevent overspending, especially with credit cards. A major challenge with credit cards is that we are separated from the actual dollars being spent; just a swipe and we are done. Imagine for a second if all of your card transactions were replaced by physical money. Would it be easier to control spending in this hypothetical scenario? Odds are, yes. While changing spending methods to 100 percent cash is impractical, this thought exercise, or a budgeting program like YNAB or Mint, help make our transactions more tangible and have potential benefit through limiting spending.

Another related behavioral principle is called the endowment effect. Researchers have identified that perceived value increases when we feel a sense of ownership. For example, I may not think your car is worth that much money; but, if I were to own the exact same car, I would feel it was worth more.

When applied to savings plans, this finding helps explain why we often miss our goals. Saving money is acknowledged as important by almost everyone, but the actual practice of saving can be difficult for some, even those who make enough money. Perhaps it is no secret, some people really like to own or consume more than they like to save. This is where defined contribution plans and opt-out programs help. By making contributions before receiving a paycheck, we never "own" or see the money, so we never feel the pain of the withdrawal.

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# Can Companies Solve Workers' Money Problems?

By Rachel Feintzeig , Wall Street Journal, April 7, 2015

***Leaders of Progress Through Business provided important quotes and background information for the following article.***

Financial-wellness plans aim to help employees cut their debt and invest for retirement.

Companies are expanding their wellness programs to focus on workers' wallets in addition to their waistlines.

Meredith Corp., Staples Inc. and PepsiCo Inc., among others, have begun offering programs aimed at improving employees' financial security.

Modeled after physical-wellness programs that invite employees to lose weight or undergo health screenings, financial-wellness programs include finance classes, counseling sessions and even video games designed to help staffers pay down debt, stick to a budget and invest for their retirement.

Bosses say the programs also boost productivity, citing research findings that suggest workers under financial strain can be distracted and absent from work. Employees, though, may wonder why their employers don't just pay them more.

Several years after the global recession and a long spell of anemic wage growth, American workers still aren't happy about the state of their finances.

The most recent Labor Department jobs report shows average hourly earnings for private sector workers were up 2.1% in March from the prior year, and wages have been growing at about 2% for the past four years. Nearly 80% of workers in the U.S. and Puerto Rico are under moderate or high levels of financial stress, according to evaluations of about 40,000 workers conducted by the financial-education firm Financial Fitness Group last year.

Companies say financially stressed workers call in sick more often and may be delaying retirement. In 2013, 76% of employers said they were interested in financial-wellness programs, according to a survey by Aon Hewitt. Last year, 93% said they were planning to create or expand their efforts.

# Can Companies Solve Workers' Money Problems? Continued…

At Meredith Corp., workers who complete a 35-question "financial wellness checkup" or take a course on refinancing their mortgage earn points that can make them eligible for cheaper health plans offered by the media company.

Employees' spouses can accrue points too, says Tim O'Neil, the company's director of employee benefits and wellness. In 2014, 80% of Meredith's 5,200 employees and spouses completed at least one workshop, and 95% filled out the questionnaire, which asks whether the person is behind on bills and whether financial stress affects their productivity at work.

Since the program began, employees' financial stress has abated at a pace that Mr. O'Neil says reflects more than just the improvement in the economy. The company says employees' focus at work has improved, too. According to Meredith surveys, 88% of workers who reported less money stress used no sick time last year, a figure that was 10 percentage points better than for those with higher levels of money stress.

As corporate-benefits programs shift more responsibility onto workers, Meredith’s chief executive, Stephen Lacy, says he hopes the personal-finance help will “empower” employees to make the right choices. “This whole self-directed activity is extremely risky without a lot of education and effort,” he says.

Others say businesses are trying to solve a problem of their own making. "Companies pulled away a lot of the social safety net that they used to provide," says Jeffrey Pfeffer, a professor of organizational behavior at the Stanford Graduate School of Business. "Since we pulled away the safety net, you of course are going to be stressed.”

In a Towers Watson report from March 2014, 76% of workers said their employer "recently enacted significant changes that could compromise their near-term or long-term finances," like scaling back retirement benefits or raising health-care costs.

"It can feel a little like 'budget better, you'll have more money’,"  says a Meredith editor in New York who spoke anonymously to avoid offending her bosses. "If I make more money, I'll have more money.“

She has also found the program "a bit big brother-y," adding:  “There’s something a little uncomfortable about the person who pays your salary knowing what margins you have.”

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# Can Companies Solve Workers' Money Problems? Continued…

Meredith says that individuals' financial information is confidential and that it views workers' survey responses only in the aggregate. Employers also say that financial wellness programs show employees that they care-and also cost less than increasing  pay.  Meredith says its program costs $100,000 a year.

Michael Case Smith, who oversees a 401(k) fund that provides one-on-one financial counseling to participating workers, says the counseling provides a "perceived benefit" to workers. "Anything [companies] can deliver that gives the employee the feeling that the employer cares for them …is timely," he says.

Mike Kelly, who runs a general-contracting business in Chicago, added the financial wellness 401(k) for his employees last year. During the recession, some workers requested loans from their plans to make ends meet. He worries about employees being distracted on the job- a potential safety issue- because of financial stress but says he can't afford to increase wages.

"If pay is holding steady, what else can you offer them?" he asks. "We haven't given out pay increases, but we can say, 'Hey, we've got a way to manage your money more efficiently.'"

At Pepsi, about 15 counselors from PricewaterhouseCoopers LLP are on hand to help employees who want to take a class on foreclosure or need help navigating insurance claims after natural disasters. "The counselors also keep management apprised of what, generally, is on employees' minds," says Chad Ryan, the company's director of compensation and benefits.

As mentioned  in last month's news letter, adding some levity to a dry topic, Staples has created videogames that teach workers about money. For example, "Bite Club," a vampire-themed game, shows players how to save for retirement. Despite some eye-rolling, the office-supplies retailer says, about $15,000 associates have played it.

Raymond Sablan says the fun of competing against co-workers, plus a character that reminded him of the popular "Twilight" series, was the "bait" he needed to start a 401(k) a few years back. Now a manager at a Texas Staples, he says he regularly urges his direct reports to play.

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# The Silver Lining in 401(k) Supreme Court Decision

Eben P. Colby, Michael S. Hines, David C. Olstein, and Seth M. Schwartz

ebn, Employee Benefits News, May 2015

On May 18, 2015, a unanimous U.S. Supreme Court held in *Tibble v. Edison International* that fiduciaries who select investment options for 401(k) plans have a continuing duty under the Employee Retirement Income Security Act of 1974 to monitor their selections and remove imprudent investment options.

The Court vacated a ruling by the U.S. Court of Appeals for the 9th Circuit that dismissed certain claims brought against fiduciaries of the Edison 401(k) Savings Plan as untimely because they related to investment options that were selected for the plan more than six years before the complaint was filed. Although the Supreme Court declined to define the precise contours of the duty to monitor, the ruling opens the door to claims challenging the prudence of plan fiduciaries' retention of investment options within 401(k) plans, including options that were selected outside the limitations period established under ERISA.

ERISA imposes on a fiduciary of an employee benefit plan — including any person responsible for selecting or removing investment options offered under a 401(k) plan — a duty of prudence that requires the fiduciary to "discharge his duties with respect to a plan ... with the care, skill, prudence, and diligence" that a prudent person would use under similar circumstances. A plan fiduciary that breaches this duty of prudence may be held liable to the plan for any resulting losses. ERISA authorizes the Department of Labor, plan participants and beneficiaries, and other plan fiduciaries to bring a civil action against a fiduciary that has acted imprudently, in order to recover such losses on behalf of the plan. Civil actions generally must be brought within six years after "the date of the last action [by the fiduciary] which constituted a part of the breach" or, if earlier, within three years after the earliest date on which the plaintiff had actual knowledge of the breach.

Participants in Edison's plan filed suit in August 2007 against Edison International and other plan officials, alleging that the defendants had breached their duty of prudence by offering retail classes of mutual fund shares as investment options when lower cost institutional share classes could have been made available to plan participants. The U.S. District Court for the Central District of California dismissed the plaintiff's claims with respect to three mutual funds that had been added as investment options under the plan more than six years before the complaint was filed. The District Court ruled that the claims were time barred because the plaintiffs had failed to establish that the circumstances relating to those investments had changed to such an extent that a prudent fiduciary would undertake a full-scale due diligence review of the investments within the six-year limitations period.

# The Silver Lining in 401(k) Supreme Court Decision, Continued…

On appeal, the plaintiffs argued that the claims remained timely because the defendants committed a continuing breach of fiduciary duty for so long as the challenged investments remained as options within the plan. The Court of Appeals rejected this argument and affirmed the ruling of the District Court.

The Supreme Court vacated the decision and remanded the case back to the Court of Appeals for further consideration in light of trust-law principles. Justice Stephen Breyer, writing for the Court, noted that the Court of Appeals had erred by failing to recognize that under the law of trusts, from which ERISA's duty of prudence is derived, "a trustee has a continuing duty to monitor trust investments and remove imprudent ones," and that this duty exists "separate and apart from the trustee's duty to exercise prudence in selecting investments at the outset."

Accordingly, even though the challenged investments were selected more than six years prior to commencement of the plaintiffs' action, a claim alleging that the defendants failed to prudently monitor and remove the investments still could be deemed timely as long as the alleged failure to monitor occurred within the limitations period.