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To: Committee Members

From: Tara Hagan

CC: Steve Platt, ING

Robert Trenerry, Hartford

Cameron Vandenberg, Deputy Attorney General

Date: 11/8/2011

Re: Discussion Regarding Loan Provision

Background:

The Committee will continue its discussion regarding the possibility of adding a loan provision to NDC effective with the new provider contract in 2013. Staff provided the Committee with comparative information in August which included National Association of Governmental Defined Contribution Administrators (NAGDCA) survey information and Nevada 457(b) loan provision specifics from the Hartford.

The NAGDCA surveys indicate plan sponsors are nearly evenly split on those who offer loans versus those who do not. The surveys also indicate that participant usage remained fairly low (0% - 5%) even during these difficult economic times. However, information obtained from Hartford regarding Nevada specific loan usage seems to indicate higher usage than the average. The average Nevada governmental 457(b) plan usage, as provided by Hartford, noted a range of 1% - 18% of participants requesting a loan in a 12-month period versus the 0% -5% noted by the NAGDCA survey.

Administration:

As reported in August, Staff will be responsible for all defaulted participant loans. Staff will be required to contact each appropriate human resources division to more fully understand the participant's situation and make a determination regarding whether the participant is exempt from the default process based on Internal Revenue Service (IRS) guidelines.

We anticipate the workflow to remain manageable but foresee the need for a second full time employee to assist with the addition of the loan provision and continued increase in day to day activities as a result of staff communications directly to the participants and employees. This includes the extremely positive results Staff has experienced as a product of mass communicating the easy enrollment form.

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Considerations:
Although governmental plans differ from their private sector counterparts, over 80% of employer 401(k) plans offer loans and have done so since 1996. Due to the historical data that is available, it's useful to consider private sector experiences regarding the effects of loans on participant wealth accumulation throughout the years.

In 2008, the Social Security Administration (SSA) commissioned a study as part of the 10th Annual Joint Conference of the Retirement Research Consortium. The study, titled 'A Primer on 401(k) Loans' suggests 401(k) loans are 'neither a blessing nor a bogeyman'. Moreover, the paper noted loan provisions may have the subtle effect of raising net asset accumulation by making participation in defined contribution plans more appealing: employees who can access their 401(k) assets if they need them may be more willing to put more money into an otherwise illiquid account.

The study's empirical analysis suggests that it may be possible to structure the provision of loans in ways that reduce their potential to negatively impact retirement wealth accumulation, as the research found that the 401(k) utilization is responsive to the types of loan features adopted by plan sponsors. 401(k) loan utilization is higher in plans that have lower minimum loan amounts and in plans that allow employees to take multiple loans. 401(k) loan utilization is lower in plans that have higher loan interest rates.

Therefore, we must carefully consider this information as we begin to craft the loan policy. As the loan policy requires consideration of various items, such as:

- Interest Rate Determination
- Minimum and Maximum loan amounts
- Loan Documentation Processing
- Number of Loans
- Default provisions
- Collection process (via bank account debit or ACH only)

Although 401(k) loans are often described as a problem, as the research paper indicates classical economic theory has a more benign view. Loans can relax liquidity constraints and may be a reasonable source of credit in many circumstances. The study found the existence of a loan provision may also increase participation since a loan option increases flexibility of 401(k) savings.

As NDC considers the future and the next 5-year contract period, it seems the necessity of offering loans will increase. Studies indicate the larger the Plan, the more likely it is to offer loans. Staff is recommending the Committee add a loan provision to NDC effective with the new provider contract in 2013.

Recommended Motion:
Motion to direct Staff to begin drafting a loan policy, including action items and a timeline, which will be incorporated in the service provider request for proposal process and become effective in January 2013.