Market & Legal Update

SEPTEMBER 2024 REVIEW

Stay on top of the latest market developments and legal and regulatory updates that may affect your business.

MARKET UPDATE | Fed Green Lights Rate Cuts on the Horizon

After aggressively raising rates 11 times from March 2022 to July 2023, the Fed finally did what the markets had been hoping for since early in 2024: they cut their target interest rate. But that's not all. While the rate cut was widely expected at their September meeting, the size of that rate cut was the big unknown. Would they take it slow and conservative and cut rates by a quarter percent? Or would they make a splash and cut by half a percent? Much to the delight of investors, it was the latter. On September 18th, the policy-setting Federal Open Market Committee (FOMC) lowered its target range for the federal funds rate to 4.75%–5%, from the 5.25–5.5% range. Along with favorable economic data that was reported during September, the markets reacted favorably, and September proved to be a solid month returns-wise. For the month, the S&P 500 and Dow Jones Industrial Average (DJIA) gained 2.1% and 2.0% respectively, while the tech-heavy NASDAQ jumped 2.7%. International developed markets, as measured by the MSCI EAFE Index, returned 1.0%, while emerging markets, as measured by the MSCI Emerging Markets Index, surged 6.7%. Bond yields fell yet again during the month and sent the Bloomberg U.S. Aggregate up 1.3%.

Market Return Indexes	Sept 2024	YTD 2024	2023
Dow Jones Industrial Average	2.0%	13.9%	16.2%
S&P 500	2.1%	22.1%	26.3%
NASDAQ (price change)	2.7%	21.2%	43.4%
MSCI Eur. Australasia Far East (EAFE)	1.0%	13.5%	18.2%
MSCI Emerging Markets	6.7%	17.2%	9.8%
Bloomberg High Yield	1.6%	8.0%	13.4%
Bloomberg U.S. Aggregate Bond	1.3%	4.5%	5.5%
Yield Data	**Sept 2024**	**Aug 2024**	**July 2024**
U.S. 10-Year Treasury Yield	3.81%	3.91%	4.09%

The Fed continued to see inflation moving in the right direction, closer and closer to their 2% target. The Consumer Price Index (CPI) fell from 3.0% year-over-year in June to 2.9% for July, then 2.5% for August, while the Fed's preferred inflation gauge, Personal Consumption Expenditures (PCE) index, showed prices increased at a slower pace than expected on a monthly basis in August. Headline PCE was 2.2% for August vs. a projected 2.3%, moving closer and closer to the Fed's 2% target.

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The core PCE index, which strips out the volatile food and energy component, rose 0.1% from the prior month during August, below Wall Street's expectations for 0.2% and the 0.2% reading seen in July.

Moreover, the growth of the economy is also relatively strong. The third estimate of second quarter US gross domestic product (GDP) was unchanged from the second estimate, showing a 3% annualized growth rate, ahead of economists' estimates of 2.9%, and higher than the 1.4% annualized growth seen in the first quarter.

While cooling inflation made it an easier decision for the Fed to cut rates, recent employment data was likely the driving factor, as one of the first signs of recession is weakness in the job market. As the unemployment rate crept up from 3.7% at the beginning of the year to 4.3% at the end of July and 4.2% at the end of August, the Fed certainly took notice. Also, job creation numbers disappointed at the initial release dates for June and July and were revised down further. The change in total nonfarm payroll employment for June was revised down by 61,000, from +179,000 to +118,000, while the change for July was revised down by 25,000, from +114,000 to +89,000. With these revisions, employment in June and July combined was 86,000 lower than previously reported.

MARKET UPDATE *continued*

To get ahead of the slowing job market, this is likely one reason the Fed decided to cut by 50 basis points over the more conservative 25 basis point path. "The labor market is actually in solid condition — and our intention with our policy move today is to keep it there," per Fed chair Jerome Powell.

Looking ahead, projections suggest that the Fed will shift to smaller quarter-point rate cuts going forward, with the central bank projecting that the rate will be cut an additional half-point by December. This would likely mean a quarter-point cut at each of its two remaining 2024 meetings. Looking further out, Fed officials median target rate is down to 3.4% by the end of next year, which implies four quarter-point rate cuts in 2025.

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The markets received what the markets had been asking for, a cut in rates. And monetary easing typically bodes well for the stock market. Since 1974, the market has been up eight out of ten times the following year after the Fed initiated a rate cutting cycle. While some believe the Fed navigated a relatively tough environment and is on its way to a "soft landing", where inflation is reduced but economic growth is maintained, there are others that remain skeptical. The skeptics will point to the last three rate cutting occurrences where the cut was followed by an economic downturn. They may also point to the size of the rate cut and wonder if it meant the economy was in dire need of stimulus, which could foreshadow trouble brewing on the horizon. Which side is correct remains to be seen, but at this point it appears that the Fed has been able to use its policy to reduce inflation while keeping unemployment relatively tamed.

LEGAL UPDATE

IRS Issues Interim Guidance on Qualified Student Loan Payments (QSLPs)

On August 19, 2024, the IRS published Notice 2024-63 which issued interim guidance on qualified student loan payment matching contributions or a "QSLP match". As you may know, the Secure Act 2.0 permitted employers to make QSLP matching contributions for plan years beginning after December 31, 2023.

Congress intended for the QSLP matching feature to "assist employees who may not be able to save for retirement because they are overwhelmed with student debt, and thus are missing out on available matching contributions for retirement plans."[1] In general, Secure 2.0 allows employers who sponsor 401(k), 403(b), governmental 457(b) and Simple IRA plans to make matching contributions based on a participant's student loan payments, as if those student loan payments were elective deferrals to the plan.

While the Secure Act 2.0 provided a basic framework for QSLP matching contributions, the Notice provides welcome guidance to employers who wish to institute a QSLP match feature in their plan. The Notice addressed **four main questions:**

1. What is a QSLP and who is eligible to receive a QSLP match?
2. How does an employer verify QSLP match claims?
3. What reasonable procedures may a plan adopt to implement a QSLP match feature?
4. How are QSLPs treated for nondiscrimination testing?

1 What is a QSLP and who is eligible to receive a QSLP match?

A QSLP is a payment on a qualified education loan that an employee makes outside of the retirement plan that meets the following requirements. **The employee must have:**

1. A legal obligation to make the applicable loan payments
2. Incurred the loan for a qualified higher education expense of the employee, the employee's spouse, or the employee's dependent
3. Made the payment during a plan year in which a QSLP match is provided by the employer

The maximum QSLP that may be taken into account for an employee in a plan year varies based on the type of plan. In a 401(k) or 403(b) plan the QSLP limit is the lesser of the elective deferrals the employee could have contributed under IRC 402(g) (for plan year 2024 $23,000 + catch-up contributions) or the employee's annual compensation, less any actual elective deferrals made to the plan. Similar limitations apply to QSLPs under 457(b) and SIMPLE IRA plans.

[1] Secure 2.0 Section by Section Summary, Senate Committee on Finance

While nothing requires a plan sponsor to offer a QSLP match, if the plan sponsor chooses to include a QSLP match feature in the plan, the match must apply broadly and uniformly across the plan. All employees who would otherwise be eligible to receive an employer matching contribution on elective deferrals must be eligible to receive an employer match on account QSLPs. The QSLP match cannot be limited based on the type of degree, attendance at particular school, or to payments that are solely applicable to the employee's own education, and may not be limited to certain employees. For example, employees may not be excluded based on business unit, division, or location. The one exception is that a plan may include a QSLP match that applies only to non-collectively bargained employees.

2 How does an Employer verify QSLPs?

To receive a QSLP match, an employee must certify the loan payments meet the QSLP requirements. **This certification must include that the:**

1. Loan being repaid is a qualified education loan that was used to pay for a qualified education expense of the employee, the employee's spouse, or the employee's dependent
2. Employee incurred the loan

3. Amount of the loan payment
4. Date of the loan payment
5. Employee made the payment

The Notice provides that all the certification requirements may be satisfied through an affirmative certification by the employee. For example, the plan may require the employee to make an annual affirmative written certification that includes all five pieces of information needed to verify eligibility for the QSLP match.

Alternatively, the last three items listed above - the amount and date of the payment and identity of the payor, may be certified by either independent verification by the employer or passive certification by the employee. Under the independent verification method, the employer adopts a method where the plan can unilaterally validate such information, for example through the employee making QSLPs through payroll deduction.

The passive certification method is a hybrid certification method where the lender provides information to the plan regarding the dates and amounts of loan payments and the plan provides the employee with notice of the information received from the lender and gives the employee a reasonable period to correct any of the information provided in the notice. If the employee does correct any information contained in the notice, the plan may treat the employee as having certified that information as accurate.

3 What reasonable procedures may a plan adopt to implement a QSLP match feature?

A plan may adopt reasonable procedures governing the QSLP match so long as those procedures promote compliance with the QSLP match requirements and do not, in practice, limit the availability of the QSLP match to employees. Examples of reasonable procedures include quarterly or annual deadlines for QSLP match claim submissions and a plan requiring independent or passive verification procedures.

QSLP procedures may not however make the QSLP match effectively unavailable to eligible employees. *For example*, if an employee is not able to electronically provide loan data to the plan, the procedures must provide an alternative such as a participant providing cancelled checks or loan statements.

4 How are QSLPs treated for nondiscrimination testing?

The guidance permits the use of alternative testing methods for performing the Average Deferral Percentage (ADP) test for plans that adopt QSLP matching contributions. The alternative testing methods provide flexibility to ensure the QSLP match feature does not automatically create a disadvantage in the ADP test. The Notice allows plan administrators to either combine all participants for a single test or perform separate tests for those making QSLP contributions and outlines the methodology for conducting these tests.

In addition to the major topics addressed in the Notice and discussed above, there were a number of distinct points of guidance:

- A plan sponsor may add a QSLP match as a mid-year change to a safe harbor plan.
- An employer may contribute QSLP matches at a different frequency than elective deferral matches, so long as the employer contributes the QSLP match at least annually.
- If an employee's QSLP certification is later determined to be incorrect, the plan may but is not required to correct the QSLP match.

The Notice serves as an example of good faith, reasonable interpretation of Secure 2.0 provisions relating to QSLP matching contributions and applies for plan years beginning after December 31, 2024. The IRS anticipates issuing further guidance including proposed regulations that will continue to answer remaining questions plan sponsors have in interpreting and implementing the QSLP provisions of Secure 2.0

How USI Consulting Group (USICG) Can Assist

If you're interested in implementing this provision, please reach out to your USICG representative for more information and assistance. As always, the USICG Team will continue to monitor this provision and keep you apprised of any further guidance and developments related to QSLPs. USICG is also available to help answer any questions you may have regarding this topic.

Retirement Resources for You

USI Consulting Group's team of experts is happy to assist employers with all retirement plan compliance matters and changes in the market, including those discussed here, to help you mitigate risk and financial impact to your organization.

To learn more, please contact your local USICG representative, visit our Contact Us page or reach out to us at information@usicg.com.

Find the address and telephone number of your local USI Consulting Group office here.

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An index is a measure of value changes in a representative grouping of stocks, bonds, or other securities. Indexes are used primarily for comparative performance measurement and as a gauge of movements in financial markets. You can not invest directly in an index and, for comparative purposes; they do not reflect the effect of the various fees inherent in actual investment vehicles.

The S&P 500 Index is a market value weighted index showing the change in the aggregate market value of 500 U.S. stocks. It is a commonly used measure of stock market total return performance.

The Dow Jones Industrial Average is a price weighted index comprised of 30 actively traded blue chip stocks; primarily industrial companies, but including some service oriented firms.

The NASDAQ Composite Index is a market-value weighted index that measures all domestic and non-U.S. based securities listed on the NASDAQ Stock Market.

Gross Domestic Product (GDP) is the market value of the goods and services produced by labor and property in the U.S. It is comprised of consumer and government purchases, net exports of goods and services, and private domestic investments. The Commerce Department releases figures for GDP on a quarterly basis. Inflation adjusted GDP (or real GDP) is used to measure growth of the U.S. economy.

The MSCI Europe and Australasia, Far East Equity Index (EAFE) is a market capitalization weighted unmanaged index developed by Morgan Stanley Capital International to measure approximately 1,100 securities in 21 major overseas stock markets. It is a commonly used measure for foreign stock market performance.

The Barclays Capital U.S. Aggregate Index covers the U.S. Dollar denominated investment grade, fixed-rate, taxable bond market of SEC-registered securities.

The Barclays Capital U.S. Corporate High Yield Index covers the U.S. Dollar denominated, non-investment grade, fixed income, taxable corporate bond market. Securities are classified as high-yield if the middle rating of Moody's Fitch, and S&P is Ba1/BB+/BB+ or below.

The MSCI Emerging Markets Index (EM) is a free-float-adjusted market-capitalization index developed by Morgan Stanley Capital International. It is designed to measure the equity market performance of 26 emerging market countries.

The 10 Year Treasury Yield is the interest rate the U.S. government pays to borrow money for a 10-year period. In addition to influencing how much the government pays to borrow over this time-frame, the 10-year Treasury Yields also determines how much investors earn by investing in this debt and it is a good indicator of investor sentiment.

The higher the yield, the better the economic outlook.

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