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Plan Provider Sponsored IRAs Can Deliver Cost Effective Retirement Income Solutions

As defined benefit plans continue to decrease in popularity, alternative retirement income solutions are becoming more important in plan design as a means of combating America's retirement savings crisis.

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Every year, leaders in the retirement industry discuss trends they believe will shape the future. For the last few years, expectations have focused on repurposing defined contribution (DC) plans to help current and former participants transition from work into retirement. Of course, with Millennials and Gen Y headed into the heart of their working years, plan sponsors are expected to maintain traditional tools and resources that support asset accumulation. To date, relatively few plan sponsors have adopted retirement income options because the solutions have the potential to increase administrative complexity, plan costs, and fiduciary risks.

One viable option for delivering retirement income solutions to plan participants is Plan Provider Sponsored Individual Retirement Accounts (IRAs). As retirement plan providers seek ways to deliver additional value to plan sponsors and make retirement income solutions available to plan participants, there is increased interest in white-label IRAs.

Repurposing the Booster Rocket

The undisputed need to improve retirement security in the United States creates a tremendous impetus to adapt DC plans to better meet the needs of older participants. Unfortunately, that is not what DC plans were designed to do. Originally, 401(k) plans were structured as supplemental savings programs—booster rockets, if you will—that gave employees the opportunity to supplement the income their pensions would deliver.

As pension plans became less prevalent, DC plans were repurposed. Plan sponsors affixed automatic features and new investment options to their plans, improving the possibility that participants would reach targeted outcomes. The new features also added complexity and cost to plan administration. {"Retirement Income Comes into Focus for Plan Sponsors," *Pensions & Investments*, *https://www.pionline.com/article/20180903/ CUSTOM_MEDIA/180829815/retirement-income-comes-into-focus-for-plan-sponsors/R* (retrieved Feb 2019)}

Now, we are asking DC plans to evolve again by fastening on retirement income solutions. Plan sponsors have been asked to consider fresh solutions along with old standbys, including:

- **Partial Withdrawals.** Periodic withdrawals seem relatively straightforward, but adopting the feature necessitates myriad decisions for plan sponsors around timing, withdrawals, and cost. What are the fiduciary implications and potential repercussions? {Sclafani, Jessica, Worsfold, Rennie, Keith, Doug, et al., "Design Matters: Plan Distribution Options," Defined Contribution Institutional Investment Association, *https://c.ymcdn.com/sites/dciia.org/resource/collection/F3BE0E33-FB72-44A0-86A1-78B6CA99454D/Design_Matters_Distribution_25apr18.pdf* (retrieved Feb 2019)}
- **Systematic Withdrawal Plans (SWPs).** SWPs allow participants to receive periodic payments of specific amounts at defined intervals, creating streams of retirement income. Plan sponsors that adopt SWPs will need to make decisions related to the limits and responsibilities of the program. {Sclafani, Jessica, Worsfold, Rennie, Keith, Doug, et al., "Design Matters: Plan Distribution Options," Defined Contribution Institutional Investment Association, *https://c.ymcdn.com/sites/dciia.org/resource/collection/F3BE0E33-FB72-44A0-86A1-78B6CA99454D/Design_Matters_Distribution_25apr18.pdf* (retrieved Feb 2019)}
- **Managed Accounts.** Managed accounts, which provide more personalized investment strategies than target-date funds, were one of the most frequently adopted retirement income strategies. Some managed account providers provide advice, thereby imparting a level of fiduciary protection to plan sponsors. {Knowles, Kevin, Murray, Steve, "Managed accounts: The other QDIA," Russel Investments, *https://russellinvestments.com/-/media/files/us/insights/institutions/defined-contribution/managed-accounts-the-other-qdia.pdf?la=en&hash=9663CBDFC966B74B0AF4868689E287926696DFF4* (retrieved Feb 2019)}
- **Managed Payout Funds.** These have been slow to gain momentum, but so were 401(k) plans. Managed payout funds are mutual funds that deliver variable payments to investors, the amount of which reflects a variety of factors. While these funds are relatively liquid, they do not guarantee income for life. {Waggoner, John, "How to Implement the Bucket System," Kiplinger, *https://www.kiplinger.com/article/retirement/T037-C000-S002-how-to-implement-the-bucket-system-in-retirement.html* (retrieved Feb 2019)}
- **Annuities.** Annuities remain a conundrum. Plan participants and retirees have expressed clear interest in guaranteed income, yet in 2018 just 3 percent of plans offered annuities and less than 1 percent of participants purchased them. Plan sponsors remain reluctant to offer annuities because of uncertainty about the fiduciary implications, administrative complexities, and compliance issues. {"2018 Retirement Confidence Survey," Ebri.org, *https://www.ebri.org/docs/default-source/rcs/1_2018rcs_report_ v5mgachecked.pdf?sfvrsn=e2e9302f_2* (retrieved Feb 2019); "Moving the Needle on Retirement Income," *Pensions & Investments*, *https://conferences.pionline.com/uploads/conference_admin/MON_1115_Moving_the_Needle_on_Retirement_Income_022516.pdf* (retrieved Feb 2019); "The Language of Retirement," Jackson, *https://www.jackson.com/content/dam/cfk/documents/cmc19005/CMC19005.pdf* (retrieved Feb 2019)

The most recent Callan survey indicated that just one-half of plan sponsors offer retirement income solutions. The most common (18 percent) was access to a defined benefit plan, followed by managed accounts, retirement income modeling, and lifetime income calculators. Annuities as distribution options, in-plan annuities, and qualified longevity annuity contracts remain at or near the bottom of the list. {"2019 Defined Contribution Trends," Callan, *https://www.callan.com/wp-content/uploads/2019/01/Callan-2019-DC-Trends-Survey.pdf* (retrieved Feb 2019)}

In the interest of prudence, before plan sponsors add retirement income solutions, they must decide whether adopting retirement income solutions aligns with the objectives of their plans. In broad terms, plan sponsors must decide whether they want participants to keep assets in the plan up to and through retirement or take assets with them when a break in service occurs. If plan sponsors want to help participants through retirement, they must consider the potential cost and fiduciary risks. {Sclafani, Jessica, Worsfold, Rennie, Keith, Doug, et al., "Design Matters: Plan Distribution Options," Defined Contribution Institutional Investment Association, *https://c.ymcdn.com/sites/dciia.org/resource/collection/F3BE0E33-FB72-44A0-86A1-78B6CA99454D/Design_Matters_Distribution_25apr18.pdf* (retrieved Feb 2019)}

In 2018, Drinker Biddle's Fred Reish explained,

> …the greatest impediment to the continuing inclusion of retired participants in defined contribution plans, and to the introduction of new products and services into those plans, is the fear that plan sponsors have of being sued for a fiduciary breach. That fear includes: possible increased damages where retirees continue to have money in a plan; claims of fiduciary breaches where a plan sponsor changes to another recordkeeper, resulting in a loss of guaranteed benefits; and litigation about annuities provided by insurance companies if their financial condition weakens. As a result, plan sponsors prefer safe harbors where compliance is objective and obvious.

{Reish, Fred and Ashton, Bruce, "Written Statement to the Employee ERISA Advisory Council Lifetime Income Solutions as a Qualified Default Investment Alternative Focus on Decumulation and Rollovers," US Department of Labor, *https://www.dol.gov/sites/default/files/ebsa/about-ebsa/about-us/erisa-advisory-council/2018-lifetime-income-solutions-as-a-qdia-reish-written-statement-08-15.pdf* (retrieved Feb 2019)}

In the interest of making solutions available sooner rather than later, it may be time to consider the role of IRAs in providing retirement income. Many of the retirement income options plan sponsors are being encouraged to adopt are available through IRAs.

The primary objection to IRAs has been cost. In fact, a key benefit of offering retirement income options through defined contribution plans is lowering cost for participants. The purchasing power of plans, typically, is superior to the purchasing power of participants. However, institutional investment pricing often is available to participants through Plan Provider Sponsored IRAs, as are many of the retirement income solutions DC plan sponsors are being encouraged to adopt. {Reish, Fred and Ashton, Bruce, "Written Statement to the Employee ERISA Advisory Council Lifetime Income Solutions as a Qualified Default Investment Alternative Focus on Decumulation and Rollovers," US Department of Labor, *https://www.dol.gov/sites/default/files/ebsa/about-ebsa/about-us/erisa-advisory-council/2018-lifetime-income-solutions-as-a-qdia-reish-written-statement-08-15.pdf* (retrieved Feb 2019)}

The industry's focus on retirement income, along with the challenges created by service provider consolidation and fee compression, have been responsible for the rising interest in white-labeling IRAs. It is a cost-effective way for providers to build and market proprietary IRAs. Service providers can seamlessly integrate plan distribution requests and IRA account establishment processes to minimize participant inertia—and the entire process can be completed digitally.

White Labeling provides flexibility so plan providers can select the level of service they want to deliver. If the company wants to build relationships with former plan participants in the wealth management space, it can choose to have a dedicated call center and custom Web portals. If a provider prefers a participant-initiated rollover process, it can establish links or participant Websites.

The win-win-win solution benefits providers, plan sponsors, and participants. Capturing assets in IRAs gives service providers the opportunity to retain and grow assets under management and to preserve and expand margins. Delivering institutional share class pricing and diverse income options helps plan providers reduce the pressure on plan sponsors, while giving participants the opportunity to invest in strategic allocations of familiar funds, purchase immediate and deferred annuities, or participate in other types of retirement income opportunities.

Improving retirement security in the United States is critical. As we pursue this goal, we need to remain cognizant of the responsibilities and risks we are asking plan sponsors to accept. Plan sponsors do not need to do all of the heavy lifting. Service providers also can deliver retirement income solutions through IRAs. ■