Defined Contribution Institutional Investment Association

Dedicated to Enhancing Retirement Security

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Why Now?

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Defined contribution (DC) plans, designed to help workers achieve a secure retirement, have become a critical linchpin of the private and public sector benefit systems. Having evolved meaningfully over the past 40 years, today's DC plans now enable participants to accumulate and invest retirement assets even more easily than in the past. In addition, these plans cover far more individuals than the defined benefit (DB) plan system did, even at its apex. They also allow participants to retain assets that they have accumulated through a multi-employer career, though these may still be scattered across multiple plans.[1]

For example, people age 50+ who have participated in DC plans throughout their working years now have accumulated substantial balances — approximately $300,000, on average.[2] Yet research indicates that most of them are ill-prepared to convert their assets into retirement income. As one study succinctly states, "People do not even know what questions should be considered."[3] The conclusion for DC plan sponsors seeking to assist these participants is clear: the next step is to evolve their plan's design and investments further to simplify the creation of retirement income. By adding a benefit distribution focus to their plan's offerings and communications and/or services to better address the needs of those near or in retirement, they can create what is known as a "retirement tier" for their plan —an enhancement that can ultimately also benefit the employer and the plan itself.

The retirement tier encompasses a range of products, solutions, tools, and services, all of which allow a DC plan sponsor to potentially better support participants who are near, entering, or in retirement.

IT'S A NUMBERS GAME

10,000	Number of baby boomers in the US turning 65 each day[4]
73 million	Number of people aged 65+ by 2030, up from 49 million in 2016[5]

Trendline: A growing dependence on DC plan *assets* rather than pension *income*

RETIREES WILL LIVE LONGER

Today, a 65-year-old male can expect (on average) to live to age 84. A female can expect to live to age 87.[6] This increased longevity makes it vital that participants receive informed and thoughtful guidance on creating a spending plan for their accumulated DC plan savings.

PRE-RETIREES: TOO MANY TO IGNORE

Employees age 50 and older:

- Have the **longest average employment tenure** of all age groups[7]
- Are **less likely to change jobs** as they approach retirement
- May **delay retirement** if in doubt about financial security

According to Prudential, for each year that a participant delays retirement, it costs their plan sponsor $50,000 in incremental benefits.[8]

EARLY SOCIAL SECURITY CLAIMING IS COMMON

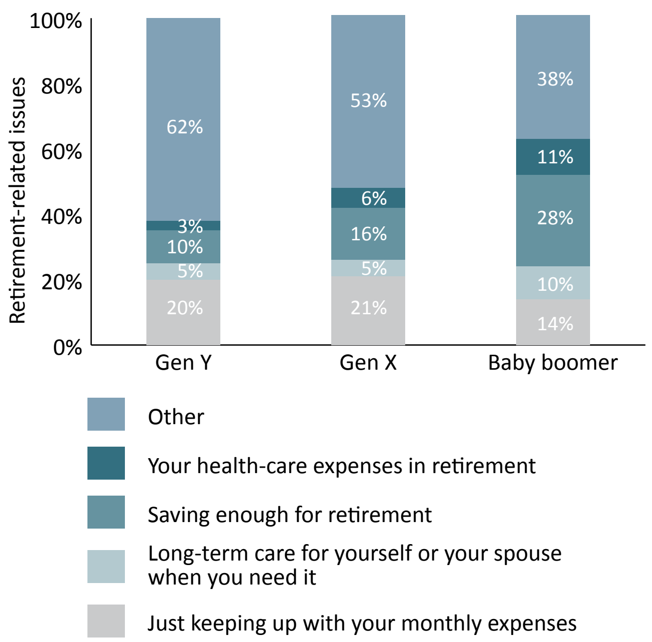
Social Security plays an enormous financial role for most retirees, yet roughly 90% make a claim prior to reaching the age for full benefits.[9] This decision seems to indicate that retirees may not understand how to optimize their Social Security benefits.

The numbers highlighted in these findings reinforce one conclusion: employees with DC assets would benefit greatly if plan sponsors provided them with the tools to transition to retirement successfully.

THOSE APPROACHING RETIREMENT NEED HELP

Worries about retirement naturally become dominant as participants age. Approximately six in 10 of them who are considering preparing for retirement report that they find doing so stressful.[10] Those who have done some retirement planning, however, report a noticeably lower degree of concern.[11]

What's Your Biggest Financial Worry Right Now — The Problem That Keeps You Awake At Night?



Source: Mercer

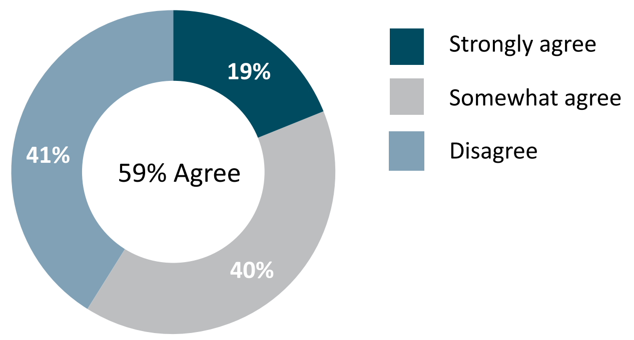
Many employers have adopted financial wellness programs with the goal of reducing the financial stress that their employees experience. Facilitating retirement planning through adding a retirement tier can help reduce financial stress and therefore can also help employers achieve their financial wellness programs' goals.

RETAINING RETIREE ASSETS MAY OFFER BENEFITS TO PLAN SPONSORS AS WELL AS PARTICIPANTS

Economies of Scale Can be Powerful

Participants age 50 or older control 63% of all plan assets.[12] Retaining these participants' assets even after they retire can assist DC plan sponsors in achieving and retaining plan economies of scale. As a plan loses larger accounts, both its total size and the average size of its individual accounts decline. All else being equal, such losses work against securing lower recordkeeping and investment management fees for all employees, whether active or separated.

Preparing For Retirement Makes You Feel Stressed



Source: EBRI Retirement Confidence Survey 2018

Corporate Reputation, Talent And Workforce Management Can Be Supported

An organization's reputation as an employer is important to consumers and affects its ability to attract top talent. Satisfied employees are more likely to praise their employer to their friends and contacts, conferring a recruiting advantage on that employer in today's tight labor market.[13] A 2016 GAO report identified steps that DC plans can take to improve retirement income options for participants.[14] It found that employees look for help planning for retirement income not only at retirement, but also in the years leading up to it. Unfortunately, the GAO reports, a sample of 16 separation packages lacked most of the communications elements employees consider critical; the report found that employees consider the separation packages their employers provide at retirement particularly important.

It is vital to ensure that separating participants make appropriate decisions about how to handle their distributable plan assets because:

- The decision to take a lump-sum distribution is irreversible — assets moved out of the plan cannot move back in
- Assets distributed from the plan lose the plan's fiduciary protections
- Assets rolled into Individual Retirement Accounts (IRAs) may result in higher fees

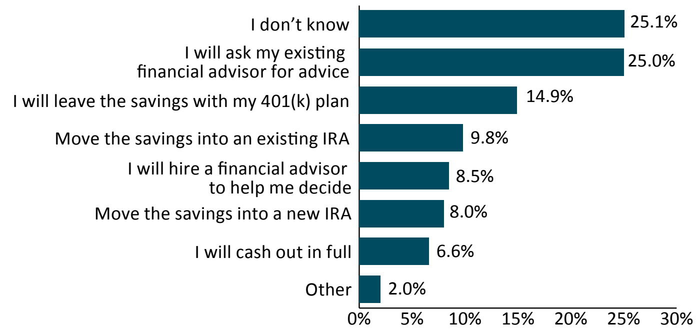
Employers who make retirement a less-intimidating prospect for participants may reap the benefit of improving workforce management, since proactively assisting near-retirees helps to avoid having less-engaged, older employees.

COMPLEX DECISIONS WITH LASTING CONSEQUENCES REQUIRE APPROPRIATE TOOLS

In part due to the transition over the years from defined benefit (DB) plans to DC plans and IRAs, many individuals do not know how to plan for using their savings when they arrive at retirement, as indicated in the bar chart below. This should not come as a surprise: the retirement-income decision is incredibly complex and requires analysis of multiple scenarios and alternatives in order to make an optimal choice. Some of the analysis behind that optimal choice might be addressed by a retirement tier. It might include:

- Defining a sustainable retirement income (consumption) goal as as a first step — ideally, this should include both core fixed household expenses and desired lifestyle spending
- Determining Social Security amount, start date and claiming strategy
- Determining asset allocation (stock/bond mix)
- Considering an annuity purchase: timing, amount, type
- Identifying an asset location and tax-efficient drawdown strategy (including Roth accounts and health savings accounts, if applicable)
- Making necessary DB plan decisions (especially for households with members who spent time in the public sector — where DB coverage remains near universal — and for whom during those years Social Security participation may have been suspended)
- Estimating future labor income — over one-third of individuals who “retire” go back into the workforce, often as self-employed or part-time employees and many at the companies from which they retired
- Examining the possible impact of personal circumstances such as changes in health, expected inheritance or existence of dependents
- Creating educational materials and communications targeted at those over age 50

401(k) Plan Participant Perspective: Intentions for 401(k) Account Savings at Retirement



Source: The Cerulli Report, U.S. Retirement End Investor 2018 — IRA owners and 401(k) plan participants

SUMMARY

As DC plans continue to evolve to better fill the need to provide sustainable income in retirement, they will naturally focus more on distribution strategies, tools and services.

The GAO recently issued a report calling for a complete re-evaluation of the retirement system; it identified the need for improved options for aiding employees reaching the retirement phase as one of its five strategic policy goals.[15] The Bipartisan Policy Center’s Commission on Retirement Security and Personal Savings came to a similar conclusion, recommending, among other things, that new rules be developed to encourage DC plan sponsors to better engage retiring and near-retirement participants in decisions about lifetime income.[16]

Virtually all constituencies recognize that those near, at, or in retirement need much more robust support than they currently receive to create and maintain retirement income. Plan sponsors who seek good retirement outcomes for their employees can do so by examining their individual plans, assessing their plans’ present capabilities, and moving forward with beneficial enhancements.

The Retirement Tier papers are a multi-part series. Other papers in the series may be accessed through the DCIIA website at **www.DCIIA.org**

ENDNOTES

[1]Employee Benefits Security Administration (EBRI), United States Department of Labor, Private Pension Plan Bulletin Historical Tables and Graphs 1975-2016, December 2018.

[2]Jack VanDerhei, Sarah Holden, Luis Alonso and Steven Bass, "401(k) Plan Asset Allocation, Account Balances, and Loan Activity in 2016," EBRI Issue Brief, No. 458, September 10, 2018.

[3]Carol A. Bogosian and Anna M. Rappaport, "What Employers Can Learn from What Retirees Say: Insights from the Society of Actuaries Research on Post-Retirement Risk," Plan Sponsor Council of America (PSCA), 70th Annual National Conference, May 2, 2017.

[4]Russell Heimlich, "Baby Boomers Retire," Pew Research Center, December 29, 2010, http://www.pewresearch.org/fact-tank/2010/12/29/baby-boomers-retire/ (accessed February 25, 2019).

[5]Jonathan Vespa, David M. Armstrong and Lauren Medina, "Demographic Turning Points for the United States: Population Projections for 2020 to 2060," United States Census Bureau, U.S. Department of Commerce, issued March 2018.

[6]Social Security Administration, "Benefits Planner / Life Expectancy," https://www.ssa.gov/planners/lifeexpectancy.html (accessed February 25, 2019).

[7]Craig Copeland, "Employee Tenure Trends, 1983-2016," EBRI Notes, Vol. 38, No. 9, September 2017.

[8]Prudential Research & Perspectives, "Why Employers Should Care About the Cost of Delayed Retirements," Prudential Insurance Company, 2017.

[9]Social Security Administration, Annual Statistical Supplement to the Social Security Bulletin 2017"

[10]2018 RCS Fact Sheet #3, "Preparing for Retirement in America," 2018 Retirement Confidence Survey, Employee Benefit Research Institute and Greenwald & Associates, April 2018.

[11]Mercer, "Inside Employees' Minds - Financial Wellness Survey," September 2016.

[12]Jack Vanderhei, Sarah Holden, Luis Alonso and Steven Bass, "401(k) Plan Asset Allocation, Account Balances, and Loan Activity in 2016," EBRI Issue Brief, No. 458, September 10, 2018.

[13]Denise Lee Yohn, "Reminder: Customers Care How You Treat Your Employees," Harvard Business Review, September 26, 2018, https://hbr.org/2018/09/reminder-customers-care-how-you-treat-your-employees (accessed October 2, 2018).

[14]U.S. Government Accountability Office, "401(k) Plans – DOL Could Take Steps to Improve Retirement Income Options for Plan Participants," Report GAO-16-433, August 2016.

[15]U.S. Government Accountability Office, "The Nation's Retirement System: A Comprehensive Re-evaluation Is Needed to Better Promote Future Retirement Security," Report GAO-19-342T, February 2019.

[16]Bipartisan Policy Center, "Securing Our Financial Future: Report of the Commission on Retirement Security and Personal Savings," July 2016.

ABOUT DCIIA

DCIIA is a nonprofit association dedicated to enhancing the retirement security of America's workers. DCIIA's diverse group of members include investment managers, consultants and advisors, law firms, recordkeepers, insurance companies, plan sponsors and other thought leaders who are collectively committed to the best interests of plan participants. For more information, visit: **www.dciia.org**.

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