

# How you can help your defined contribution plan participants in 2020

Defined contribution (DC) plan assets have soared in recent years, rising about 90% between 2007 and mid-2019<sup>1</sup>. And we believe they are only set to climb further as defined benefit plans continue to decline and employers turn to DC plans as the sole source of retirement income for their employees. This trend is driving more innovation, more focus on compliance and competitive fee structures.

This article suggests action steps in three broad areas – financial wellbeing, investment trends, and plan compliance – to help DC plan sponsors address the challenges of 2020 and beyond.

## Financial wellbeing



### Measure workforce financial stress

Achieving retirement security is a shared responsibility between employers and employees. But employees can't do their part if they have competing financial obligations and are unable to save for retirement. Effective financial wellbeing programs can help remove financial barriers employees face. But before rolling out a program, employers should first measure the financial stress of their workforce.

Leading employers have taken several steps to gauge the financial needs of their workforce. Focus groups and pulse surveys help employers understand employee preferences. And detailed workforce analytics can provide a view into which employee segments are financially struggling and why. By identifying employee preferences and needs, sponsors can remove the guesswork and adopt financial wellbeing solutions that can create value and be broadly used by its workforce.



### Consider decision-support tools and financial coaching

Retirement planning technology has come a long way since the days of simple DC account projection tools. Today's leading-edge solutions focus on decision support and build on recent learnings from behavioral economics and employee attitude research. Willis Towers Watson research finds that most employees prefer dynamic spending and savings tools over static budgeting tools. Employees want to be nudged, not judged. And they want decision support tools that provide personalized and actionable suggestions – without a lot of required data entry.

Research shows that employees also want unbiased financial coaching. Willis Towers Watson's 2017/2018 Global Benefits Attitude Survey indicates that employees across all cohorts overwhelmingly prefer personal advisor support to educational seminars.<sup>2</sup> When evaluating financial coaching firms, plan sponsors should consider those that have no conflict of interest, employ holistic solutions, leverage technology, and provide access to experienced and certified professionals.



### Explore innovative design solutions

A range of innovative design ideas have begun to emerge in response to the problem of workforce financial stress. The design innovations focus on helping employees balance the competing needs of long-term retirement savings and near-term financial obligations.

For example, "sidecar" or "rainy day" after-tax accounts with employee automatic deposits can help employees weather a near-term financial emergency. Student loan management programs create rewards for paying down debt in the short term. Some integrate with matching 401(k) contributions to help support long-term retirement savings. And many employers are using workforce analytics to modify their auto-contribution and auto-escalation features to ensure employees are saving at a level to stay on track for retirement.

# Investment trends



## 1 Make plan investments work harder

Accumulating DC savings has become a double challenge. Saving adequate amounts is difficult for those employees under the financial stresses discussed above. Additionally, with slow economic growth combined with near record-low interest rates and high valuations of publicly traded equities, we believe forward-looking returns in the capital markets are not expected to stand up to the past 10 years. Accordingly, superior investment selection will be essential for plan participants to help meet their retirement goals.

The asset mix in today's DC plan portfolios is dominated by publicly traded equities and fixed income, as well as liquid short-term investments. Large asset owners often allocate to diversifying assets, such as direct real estate, public equity and hedge funds, to unlock potentially superior investment returns. DC plans are the only category of institutional investors where such assets are absent. Historically this was understandable due to their illiquidity, pricing, fees and governance requirements; however, sponsors, consultants and investment managers can now judiciously add these asset classes to further diversify the current generation of target-date funds (TDFs) while enhancing potential outcomes for participants. In 2018, [Georgetown University's Center for Retirement Initiatives](#), in conjunction with Willis Towers Watson, extensively studied the value of increased diversification in TDFs, finding a significant potential improvement in outcomes for DC participants without an increase in the complexity of the participant experience.<sup>3</sup>



## 2 Design a sustainable plan to fit future growth

As DC plans gain ever more scale, plan sponsors should continue to reevaluate how they use their scale and governance to improve plan investments. Sophisticated, state-of-the-art investment options such as white label funds and custom TDFs are found today in about 65% of large plans.<sup>4</sup> Additionally, offering institutional portfolio management, low cost and flexibility in oversight, white label funds were initially available only to the largest plans. Through technology, however, providers have been able to make them accessible to smaller plans as well.

Competitive forces should spur further evolution of products for the DC marketplace. In investment management, heated competition can chip away at fees. Among administrators and asset managers, new product designs such as hybrid qualified default investment alternatives are emerging to better meet the different needs of younger and older workers. Participants will be the long-run winners in these battles, but only if sponsors monitor the progress and react to the new opportunities.



## 3 Assess the innovations occurring in DC plans to ensure they are the most sustainable for employees in all stages of life

We believe the evolution of DC plans will include broader offerings of retirement income solutions, whether as in-plan investment options, core menu offerings or guaranteed products available outside the plan. Sponsors show an increasing interest in encouraging participants to remain in their plans after they retire, with benefits for both parties. To keep retired workers onboard, suitable investments will be needed.

The SECURE Act, discussed later in greater detail, is expected to provide safe harbor cover for sponsors to offer in-plan annuity products. But regulation aside, a complete retirement offering likely will be more complex than investments applied to participants' savings efforts, as the goals and needs of retired employees rapidly diverge. While insufficient retirement savings continues to be an issue, let's not forget about those who have saved and planned appropriately, and that the risks within an individual's retirement plan creates a level of complexity that many people struggle to fully comprehend. We encourage plan sponsors to look at the available retirement income solutions that can help participants balance income needs with growth potential.

## Investment trends (continued)



### Delegate investment choices to an OCIO

Governance of DC plans grows more challenging each year, in a benefit environment expanding with new structures such as sidecars and health savings accounts, and increasing resources devoted to financial wellness. The complexity of investments is increasing as well, as discussed above. To ensure consistently high fiduciary standards, we believe sponsors should consider delegating responsibility for constructing and monitoring these more sophisticated solutions. We suggest delegating investment decisions to either internal staff with appropriate expertise or an outsourced chief investment officer (OCIO).

Utilizing an OCIO hands over investment selection and performance monitoring to dedicated specialists, allowing for better leveraging of outside expertise to drive potentially better returns, enhanced risk management and potentially lower costs due to an OCIO provider's scale in the marketplace. Employing an OCIO also frees up plan sponsor resources for advancing participant outcomes and the strategic vision of the plan.

## Plan compliance



### Conduct fee and service benchmarking

Lawsuits claiming excessive DC plan fees, overlapping and underperforming investments, and failure to monitor revenue sharing have become a fixed part of the DC plan landscape. The legal challenges began with 401(k) plans but have since spread to 403(b) plans in the tax-exempt sector.

To help address this risk, we believe plan sponsors should conduct regular fee and service benchmarking reviews. Ideally, the comparison should be against comparable plans that have recently undergone a recordkeeper search. The benefit to participants is potentially lower fees and expanded services. For plan sponsors, we believe benchmarking demonstrates that fee levels are reasonable and that they are meeting their fiduciary responsibilities.



### Adopt controls to minimize cyber risk

DC plans can be vulnerable to cyberattacks on several fronts. Whether it's a data privacy breach or a direct attack on participant accounts, the stakes are enormous for participants and plan sponsors alike. For the most part, these vulnerabilities are outside of a plan sponsor's direct control, so sponsors should conduct an independent cyber risk assessment.

This typically involves requests for information from DC vendor partners. The assessment should focus on the vendor's critical systems, remediation protocols, workforce training and overall financial commitment to cybersecurity. Sponsors should also look to outside experts who can help evaluate controls, identify security gaps, review contract language, assess insurance coverage and benchmark vendor capabilities against other providers. Like any other fiduciary obligation, reviews of cybersecurity should have a place on plan committee agendas and be thoroughly documented.

# Plan compliance (continued)



## Prepare for the SECURE Act

Retirement plan sponsors have patiently anticipated the passage of the Setting Every Community Up for Retirement Enhancement (SECURE) Act since mid-2019. Demands from a few Senate holdouts stand in its way, but enactment could help sponsors significantly improve the effectiveness of their DC programs.

The act contains 20 sections and covers a broad range of areas. Notable plan design provisions would allow penalty-free distributions for birth or adoption expenses, increase the minimum required distribution age from 70½ to 72 and increase the auto-escalation safe harbor limit from 10% to 15% of pay. The act also contains some potentially industry-altering changes. For example, unrelated employers could participate in a joint DC plan to reduce plan expenses and governance burden associated with sponsoring a plan independently; plan sponsors could receive fiduciary protection related to annuity provider selection, and part-time employees would have expanded access to DC plans.

Even with near unanimous support in Congress, the SECURE Act might not pass in the near term, but its impact could be dramatic, so we suggest plan sponsors become familiar with the Act, evaluate its opportunities and consider its impact on long-term planning. In some cases, sponsors will need to refresh their viewpoints, and in others, start thinking along entirely new lines.

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<sup>1</sup> Investment Company Institute, "US Total Retirement Market Assets", September, 2019 [https://www.ici.org/research/stats/retirement/ret\\_19\\_q2](https://www.ici.org/research/stats/retirement/ret_19_q2)

<sup>2</sup> Willis Towers Watson 2017/2018 Global Benefits Attitudes Survey, November, 2017

<sup>3</sup> The Evolution of Target Date Funds: Using Alternatives to Improve Retirement Plan Outcomes, Georgetown University Center for Retirement Initiatives, June 2018

<sup>4</sup> 2017 Willis Towers Watson Defined Contribution Plan Sponsor Survey, February 2018

## About Willis Towers Watson

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