Helping Employees Make Better Retirement Decisions

A primer on the types of advice, guidance, and education available and how to choose the best fit for your participants.

By Anna M. Rappaport

Defined contribution (DC) plans have become the dominant form of retirement plans in the United States. Research by the Society of Actuaries (SOA) and others has repeatedly demonstrated gaps in retirement knowledge and literacy. If employees are given a wide range of choices and left on their own, many will not save enough for retirement and they will not make optimal decisions to support retirement security. Concerns about retirement security are increasing in light of the combined effect of the large number of Boomers reaching retirement age, the growing costs for health care which have crowded out retirement savings, and relatively flat wages for much of the workforce. All of these issues create challenges to retirement success.

Over the last 20 years, the SOA has sponsored an extensive program of research designed to improve understanding of management of the post-retirement period.

Plan sponsors generally want to get the most value they can from the dollars they spend on benefits and they generally want their employees to achieve retirement security from the plans they provide. The purpose of these reports is to help plan sponsors improve the value they get from their plans.

Types of Retirement and Investment Advice and Decision Support

The project team defined a spectrum showing the movement toward advice. Three types of strategies were identified that represent the foundation for informed decision-making. They do not constitute what the Guide describes as personalized advice, but they are important steps in helping participants.

- **Education, financial wellness, and retirement readiness support** refers to services that inform participants about plan features, investment options and, in many cases, related areas such as financial terms, retirement planning, retirement literacy, and retirement wellness. Plan sponsors or outside plan providers often supply these services. Sometimes they partner with third-party retirement education specialty firms.
- **Automatic features** include auto-enrollment, auto-escalation, and auto-rebalancing mechanisms. Their purpose is to help DC participants grow savings even if they do not know much about the plan. The participants who do not opt-out of the automatic features can expect to fare better than those using haphazard approaches. Such features automatically enroll workers into the plans, automatically increase the workers' contribution percentages (usually annually), and automatically rebalance investments between accounts on a periodic basis. Plan sponsors choose the design of the features, and participants can opt-out.
- **Default investment** is a feature that directs employee contributions into a pre-determined option, usually following the regulations for a Qualified Default Investment Alternative (QDIA). The participant electing the default does not make his or her own investment selection among various fund offerings

During the last two years, employer-sponsored investment and retirement advice became a new focus of the SOA work. The new Society of Actuaries publication, ***Investment and Retirement Advice: A Guide for Employers,*** defines a range of approaches related to improving retirement decisions. It also defines key questions for the employer to consider in deciding which approach will be best for their specific situation. The report was preceded by a background research paper. The reports are "Models of Financial Advice for Retirement Plans: Considerations for Plan Sponsors" and "Investment and Retirement Advice — A Guide for Employers."

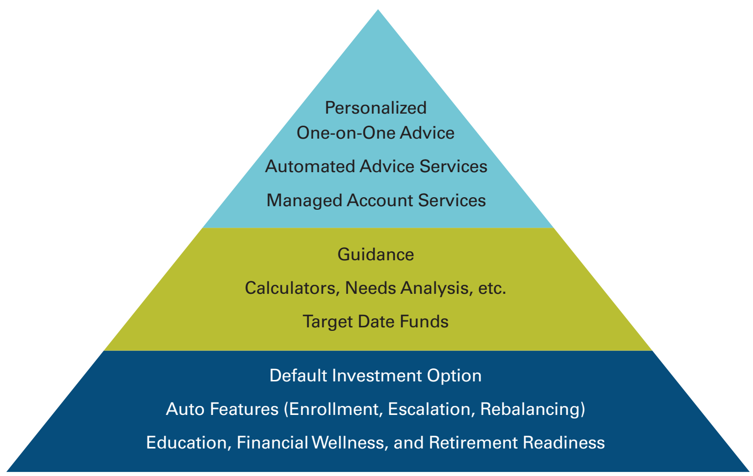
The next three categories of strategies to help participants achieve better outcomes have elements of personalized advice, to the point that some plan providers do consider one or more of them to be advice options, or auto-advice options.

- **Target date funds** are professionally-managed investment options that gradually adjust the asset allocation to more conservative options as the participant approaches the selected retirement year. Some people consider these funds to be a type of advice because the participant chooses the target retirement date based on his or her own intended retirement date. There are no recommendations to the participant, so this is not personalized advice as described in the SOA Guide.
- **Calculators** and software tools can be designed to help employees and retirees answer a number of questions. There are many types of calculators and they use different inputs and assumptions. Some give projections on how long a person might live. Others compute the impact of compound interest, loans taken, savings percentages, extended retirement dates, household assets outside the plan, and more. Calculators and software tools provide somewhat personalized advice, based on information the participant supplies — such as how much a person needs to save — but they usually do not provide recommended courses of action.
- **Guidance** is a service that helps identify areas to think about given a participant's unique situation, but without recommending specific steps such as which funds to select or how to allocate funds among them. Some employers are very comfortable providing guidance but not advice.

The last three categories are strategies that provide personalized advice in the full sense of the term. Some plan sponsors may decide to add such a service in addition to offering education, guidance, or other services. If such services are provided, they can be paid for by the plan sponsor, the participant, or on a shared basis.

- **Managed account services** make investment and portfolio decisions on behalf of plan participants who elect the option. This is not an investment option in the sense that a target date fund is an investment option. It is essentially a "do-it-for me" type of advice service. The managed account firms professionally manage the investments based on each participant's unique information.

The Movement Toward Advice



Source: Society of Actuaries

- Automated advice services, also called robo-advisors, provide an online personalized advice service. The participants enter requested data about themselves, plan assets, perhaps other assets, retirement goals, and so on. The service then computes and delivers personalized recommendations, having to do with investments and even, sometimes, retirement planning. This advice can be updated regularly or as requested. The services vary substantially, so plan sponsors need to compare and contrast the offerings carefully.
- **One-on-one advice** is a service in which a credentialed financial advisor talks with and works with a plan participant one-on-one to provide personalized advice. Depending on services elected, the exchanges can occur face-to-face, over the telephone, in call center contacts, and/or in web conferences or other online venues. The advice can range from recommendations concerning specific events, such as home purchase, to recommendations concerning in-plan investing, outside investments, retirement planning, and even ongoing retirement advice once a participant retires. The individuals offering the advice can be sales people, fiduciaries or both. Whether or not a fiduciary standard applies is a key question for the employer to explore in determining if they wish to offer a service.

Within the framework of advice models, there is, again, a spectrum:

- Automated advice only: Plan participants input data into automated software that provides specific recommendations, but does not provide individualized support.

- Automated advice plus very limited one-on-one help: Plan participants input data into automated software that provides specific recommendations, and obtain ad hoc support from a financial call center.
- Automated advice plus more one-on-one help: Plan participants input data into automated software that provides specific recommendations, and obtain support from an individual at the advice provider.
- Financial advisor provides one-on-one advice on an "ad-hoc" basis or when requested.
- Financial advisor develops and regularly updates a participant's financial plan using a systematic process.

NOTE ON LEGAL ISSUES: It is important to note that there are a variety of different laws and regulations that define what is and what is not advice and provide guidance with regard to fiduciary liability. The background paper underlying the Employer Guide includes a fairly extensive discussion of the legal background. Each employer should get guidance from their legal counsel on how the legal issues apply to them.

How Do Advice, Education, and Guidance Differ?

Advice, education, and guidance services may be referred to interchangeably. In general, however, the services have important distinctions.

- **Education services,** as noted earlier, help participants learn about plan-related matters such as investment options, contributions, and allocations. Many programs also cover more general topics such as saving, establishing retirement goals and objectives, understanding investment risk and return, getting ready to retire, what families typically do, and maintaining financial wellness (behavior that supports financial health). They do not, however, recommend that participants take specific steps.
- **Guidance services** have elements of personal counsel. For instance, given a participant's unique situation, some guidance programs might nudge a participant to consider reevaluating exposure to equities or contribution levels. Other guidance services may offer to evaluate one's personal situation, suggest options and/or respond to personal questions. Think of it as decision support that stops short of providing recommendations about what a participant should do.
- Advice services make specific recommendations for a participant based on an evaluation of the person's circumstances, needs, goals, and related matters.

Considering Different Types of Advisors

There are a variety of different types of advisors, organized in different business models, and subject to different licensing and legal requirements. The employer who decides to offer advice will need to perform due diligence in choosing the advisor. The report offers a list of questions to consider and there are more in the background paper. Some examples include:

- How is the advisor regulated?
- Does the advisor check out well with several services offered for evaluating advisors?
- Will the firms offering advice provide examples based on "test cases" supplied to them?
- Can the advisor provide samples of his or her output?
- Does the advisor's firm have a strict quality control and compliance process?
- How do the credentials pertain to the proposed delivery of advice?
- What are the sources of the advisor's compensation, and is each disclosed to the participant?

It should be noted that there is no consensus among experts on the right answers to many retirement planning questions, so that different advisors will offer different solutions and approaches. Different automated advice and software packages may also offer different approaches. Calculations are very dependent on the assumptions and the data input. Quality control over data and assumptions is also likely to vary. The use of a standard set of "test cases" in due diligence is one way to understand what participants are likely to see.

Scope of Services

Within each of the models for providing support for decisions, there is a big question of scope of the services to be offered. The paper offers some questions to consider. Again, here are some examples:

- For what types of decisions do we want to provide help?
- Does the service include the participant's total portfolio and the portfolio of all household members?
- If employees want additional services, can they buy them through the same source?

The scope questions apply to both guidance and advice, and also to the choice of software.

What Else is in the Employer Guide?

The employer guide is set up to include information to help develop the business case for advice, and to define the differences between retirement and investment advice. Some key points include:

- Plan participants need advice, and it may help reduce the number of questions they ask.
- Advice may help reduce the stress and confusion about plan decisions

and enable employees to focus more on their jobs.

- Retirement advice focuses on questions like when should I retire, when should I claim Social Security, and how should I use my resources after retirement to replace my paycheck.

The employer guide includes a discussion about the cost of advice and the different models that may be used to pay for advice services. Education and guidance may be paid for on a per-employee or per-service basis, or the cost may be bundled with other plan services. Managed accounts and other investment management services are commonly paid for as a percentage of assets. Advisors who sell products may be paid partly or totally on commissions. Fees for service can be a percentage of assets and/or a fee based on the work to be done. The guide also includes some discussion of the potential for conflicts-of-interest. It should be remembered that some types of advisors are fiduciaries and others are not. This is an evolving area and the Department of Labor has been working on the question of fiduciary standards for a long time.

Another Alternative

Employers who do not want to offer advice may wish to encourage employees to seek advice on their own and offer some information to help them find advice. Some key points for employees include:

- When one is seeking health care, there is a clear distinction between a doctor, a nurse, a physical therapist, and a home health aide. Similarly, when one is seeking retirement advice, there are a variety of professionals offering services, but the distinctions in how they are qualified and what they do is often unclear.
- However, there are some important distinctions to think about. A fiduciary is required to act in the best interest of his or her client. Some advisors are fiduciaries, but others are not. Be aware of whether or not an advisor is a fiduciary. Insurance agents and brokers may present themselves as giving advice, but they are subject to a suitability standard. They are required only to present products that are suitable for the client.
- There are several different types of licenses and regulatory regimes that apply to advisors. There are a variety of professional designations available to advisors. Some require rigorous study and examinations, but others are very easy to get.
- Some scam artists are masquerading as advisors. See the Consumer Financial Protection Board resources for some ideas on protecting against scams.
- “Retirement advice” includes a wide range of different services. It often includes advice on the management of investments. It may also include assistance in helping clients decide when to retire, when to claim social security, evaluation of whether to pay off a mortgage, advice about how much it is reasonable to spend, discussion of gifts to family members, a focus on whether housing is affordable, and even help in thinking about housing and caregiving options. Some advisors help their clients look at their total financial and life picture, whereas others are much more limited in what they do. Some sell investment and insurance products, whereas others do not sell products.

The Society of Actuaries has a decision brief “Finding Trustworthy Retirement Advice and Avoiding Pitfalls.” This publication lays out questions and considerations for choosing an advisor. It is designed for consumers and suitable to give to employees.

For More Information

The Consumer Financial Protection Bureau offers a variety of resources under the topic “Financial Protection for Older Americans.”

The CFP® Bureau’s Choosing an Advisor materials offer questions to ask and information about types of advisors and issues in choosing an advisor. The CFP® is one of the leading professional designations for advisors.

The Society of Actuaries has conducted two research studies on retirement planning software. These studies do not identify specific software but they provide an analysis of issues important to the user.

Conclusions

The SOA selected the topic of advice for these two projects and for the decision brief because of the importance of advice in improving retirement success. In planning for and executing this project, the project team discovered that there was relatively little literature on this topic. The market is growing and there are a wide variety of different types of organizations offering services. It is hoped that these reports will help plan sponsors take a systematic approach to selecting the types of decision support they wish to offer and to choosing the best option for them. It is also hoped that those who do nothing else may be encouraged to share the decision brief with employees. It is also hoped that this work will stimulate more discussion on this topic.

Anna Rappaport, F.S.A., M.A.A.A., Anna Rappaport Consulting, is an actuary, consultant, author, and speaker, and is a nationally and internationally recognized expert on the impact of change on retirement systems and workforce issues. Anna is a past- President of the Society of Actuaries and chairs its Committee on Post-Retirement Needs and Risks, which sponsored the reports on retirement advice and the Decision Brief.