The Benefits of Personalization in Defined Contribution Plans

Analyzing Value in Managed Account and Financial Wellness Programs and Features

October 2023

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Executive Summary

As the needs of plan participants shift and expand, defined contribution (DC) plan sponsors recognize that many stand to benefit from more personalized services, including financial wellness, financial planning, and managed account programs. With an array of personalized financial services and providers from which to select, plan sponsors must determine which *type* of personalized solution(s) and which solution *provider(s)* is the best fit for their plan participant base.

- Plan sponsors continue to seek out ways to make their retirement offerings more personalized to their participants' needs. With increasingly diverse participant populations, addressing the needs of participants requires programs and features that can fill in gaps left by traditional offerings (*e.g.*, target-date funds). In determining ways to make their offerings more comprehensive, personalized, and customizable, plan sponsors should consider the potential value of additional programs.

- Many plan sponsors express a preference for personalized financial solutions that offer participants the ability to speak with a financial advisor, especially for participants who have complex financial situations and planning/wellness needs. Plan sponsors should investigate the quantitative and qualitative impact of these one-on-one engagements on the financial wellbeing of their participants.

- Some plan sponsors and their consultants focus heavily on the investment performance relative to target-date fund vintages in their evaluation process. When assessing managed account programs, plan sponsors should look beyond the programs' respective investment methodologies to uncover the full impact these programs can have on participant behavior and their long-term financial outcomes.

- Some plan sponsors express concern about retirement providers cross-selling investment products, or using their workplace businesses to expand into other types of relationships with end investors. Plan sponsors should be cognizant of these conflicts of interest and actively address them with managed account providers.

Methodology

In 2Q 2023, Cerulli Associates was engaged by Edelman Financial Engines, the leading provider of workplace managed accounts and independent financial planning, to publish a whitepaper highlighting the benefits of personalization in defined contribution plans. For original research, Cerulli conducted 19 interviews with key decision makers at large (greater than $250 million in assets) DC plans, including both plans that use and do not use managed accounts. Interview topics ranged from broad themes (*e.g.*, approaches to decision-making, philosophies on plan design, driving participant engagement) to specific considerations for plan sponsors (*e.g.*, use of participant data, methods of performance measurement, approaches to addressing needs of retirees). In each interview, plan sponsors covered the effectiveness of various products and features in achieving outcomes of more personalization.

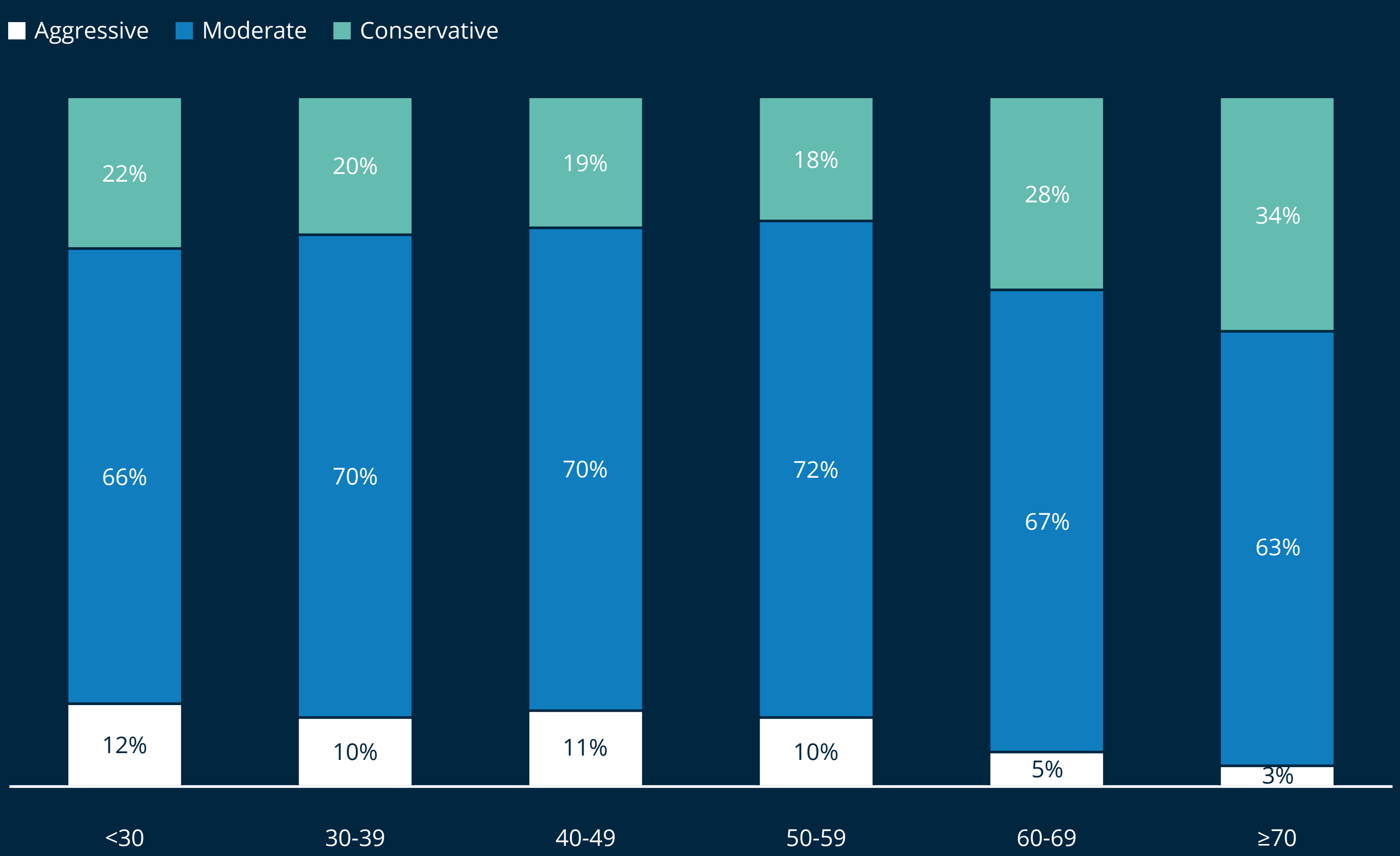
This whitepaper also draws from Cerulli's industry-leading surveys, including its 401(k) Plan Sponsor Survey, 401(k) Participant Survey and DC Consultant Survey. To maintain confidentiality, all information collected for this research is presented in aggregate form, and proprietary survey information is not directly attributed to participants or their firms.

Personalization in Defined Contribution Plans

Over the past two decades, the widespread adoption of target-date funds and automatic plan features has been decidedly integral to helping defined contribution (DC) plan participants achieve superior long-term retirement saving and investment outcomes. A major key to their success has been their simplicity—target-date funds and automatic features are designed to enhance the long-term financial outcomes of less engaged participants, partially offsetting the negative effects of investor inertia. Yet their efficacy has limitations. Helping DC plan participants achieve superior financial outcomes—in both the short term and long term—requires services and solutions tailored to their individual financial circumstances, in real time.

Most off-the-shelf target-date fund glidepaths take only one piece of participant information into consideration: age. For many participants, this results in asset allocations that are misaligned with their individual circumstances, including risk tolerances, irregular time horizons, and bespoke preferences. Certain participants have different emotional and psychological dispositions when it comes to their finances, as well as unique financial goals, which can impact their willingness to assume risk **(see Exhibit 1)**, among other saving and investing considerations. Moreover, participants' financial lives extend well beyond their current employer's 401(k) plan. They often have financial obligations that extend beyond saving for retirement, such as student loan debts, emergency savings, and their monthly bills. They also tend to have assets held in accounts outside of their current DC plan. Data from Cerulli's 2023 401(k) Participant Survey shows that 45% of participants have a brokerage account, roughly one-third have an individual retirement account (IRA), and one-in-ten accrue benefits from a defined benefit (DB) plan. Combined, these factors further reinforce the need for solutions tailored to an individual's personal financial situation, outlook, and goals.

Exhibit 1 | Investor Risk Tolerance by Head of Household Age, 2022



Sources: MarketCast, Cerulli Associates

Personalization is a prominent theme across the business-to-consumer landscape, from music and podcast streaming to grocery shopping, and workplace retirement plans are no exception. While the need for personalized guidance, advice, and portfolio management exists throughout a person's life, it is arguably most valuable to participants as they experience major life changes or achieve new milestones, including retirement. In the defined contribution (DC) market, personalized services can take several forms, but managed account programs remain the most holistic, personalized investment solution in the market today.

Personalized solutions allow participants the ability to assess and improve their retirement readiness, which is a major area of focus for plan sponsors. Data from Cerulli's 2022 401(k) Plan Sponsor Survey shows more than one-third (36%) of 401(k) plan sponsors cite improving their retirement readiness services as the top priority for their 401(k) plan **(see Exhibit 2)**.

There is a wide consensus within the retirement industry that improving participants' retirement readiness does not happen in a vacuum—a sentiment shared by several plan sponsors when expressing the role of personalization in their plans.

[With target-date funds] you're only getting one factor: age. But the 65-year-old CEO and 65-year-old security guard are completely different, so personalization is clearly very important,"

– *Head of Retirement and Benefits Strategy, Large Grocery Chain*

While managed account programs remain the premier solution for delivering personalized advice in the DC market, personalization can take many forms within workplace retirement plans, from digital, user-driven financial wellness journeys to one-on-one financial planning or coaching engagements. Plan sponsors are tasked with determining which type(s) of personalized services will be most beneficial to their participant population. Plan sponsors also must ensure that any in-plan personalized service aligns with their plan objectives and upholds their fiduciary responsibilities.

Exhibit 2 | 401(k) Plan Sponsors: Top Priority for 401(k) Plan, 2022

	Participant Age Segment			
Priority	**Younger Participant Population (≥50% Participants Are Under 40)**	**Other Evenly-Distributed Participant Population**	**Older Participant Population (≥50% Participants Are 50+)**	**All Plan Sponsors**
Improving retirement readiness education (*i.e.*, preparing employees to retire when they want to)	33%	39%	40%	36%
Improving quality of investment lineup	26%	23%	25%	25%
Adding or encouraging use of an in-plan retirement income option (*e.g.*, managed payout, guaranteed annuity)	13%	10%	14%	12%
Enhancing our financial wellness program	12%	13%	7%	12%
Reducing plan administration costs	11%	6%	8%	8%
Reviewing cybersecurity capabilities of service providers	6%	9%	6%	7%

Source: Cerulli Associates

Analyst Note: Respondents were asked for the 401(k) plan's top priority today. Data reflects responses submitted in 4Q 2022. Percentages do not sum to 100% due to rounding.

Aligning Personalized Service Offerings with Plan and Participant Characteristics

A challenge for key decision makers at some of the nation's largest corporate DC plans is selecting the *right* personalized financial service(s) for their participant base. These plans typically have sizeable, diverse participant populations with varying levels of wealth, financial challenges, objectives, and preferences. One head of global benefits for an asset management firm says, "As fiduciaries, we want to make sure the [personalized solution] delivers value and makes sense for at least some portion of our participant base." In many cases, the financial benefits available within these participant bases can vary and add further layers of complexity. For example, many of these plan sponsors offer a defined benefit (DB) pension plan or cash balance alongside their DC plan or have a legacy DB plan that has since been frozen. Lastly, since most of these plan sponsor firms are publicly traded, for swaths of their employee base, a meaningful portion of their compensation comes in the form of equity, leading to concentrated portfolios and, at times, complicated tax situations.

For these plan sponsors, offering personalized solutions that can seamlessly incorporate this information into advice, portfolio management, and guidance-based recommendations is integral.

If a participant has a DB pension or legacy pension benefit, you should be able to manage that in one place alongside their DC plan. For some participants, it's their biggest benefit. If you don't include this, the advice or projection the provider delivers is going to be totally off base."

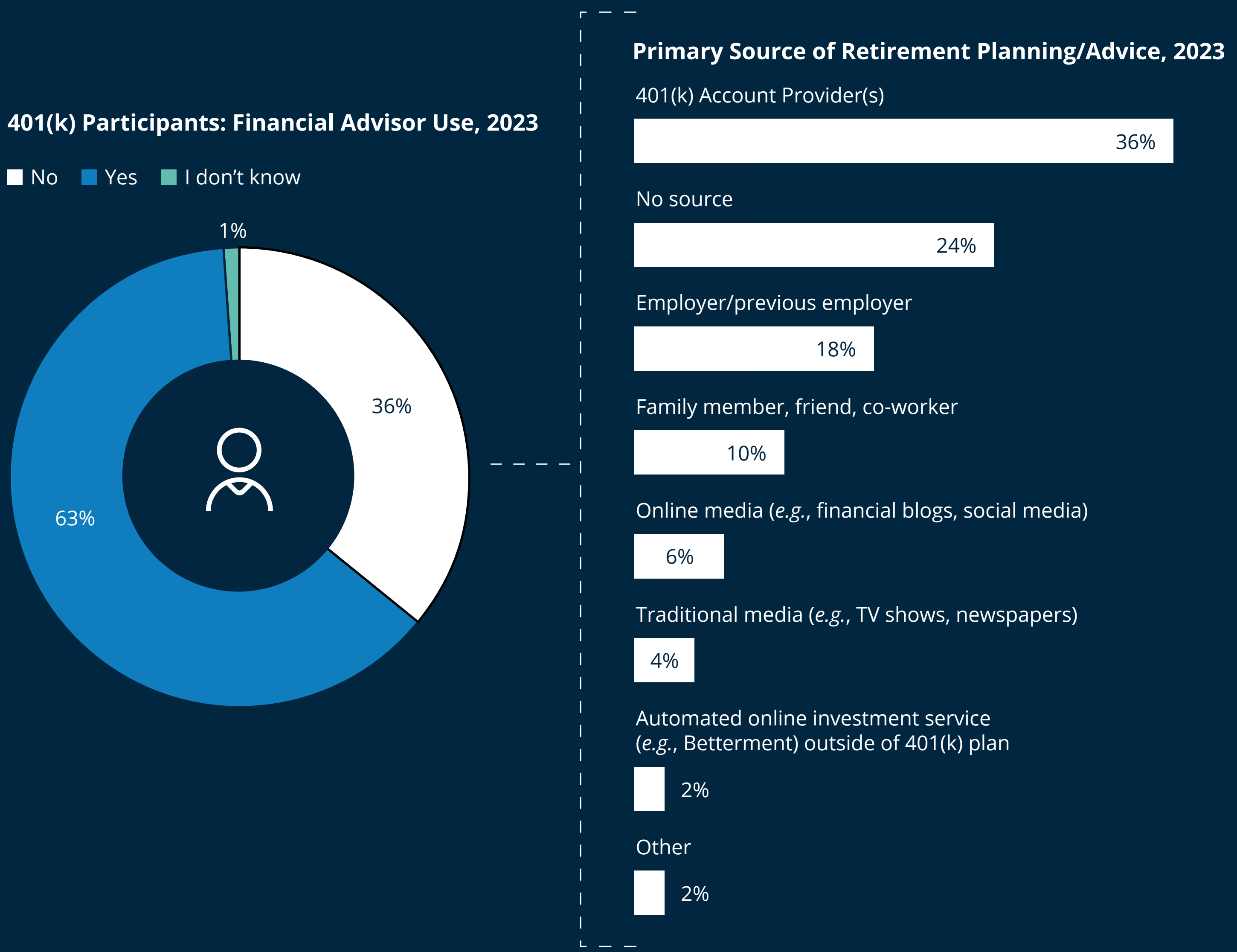
– *Pension Executive, Manufacturing Firm*

As a result of these complexities, it can be challenging to find a comprehensive solution that satisfies the needs of all participants. At times, Cerulli has observed plans with personalized financial services offerings that are not well aligned with the interests and needs of the plan's participant base. One benefits executive who helps oversee the 401(k) plan for a large manufacturing company recounts an example

of this playing out at her firm: “We have employees of varying education levels, many of whom are dealing with really basic financial problems around budgeting or, for instance, whether they should refinance their house or contribute more to their 401(k). So, we put together a financial wellness task force team and they really wanted to focus on our employees’ basic financial needs. But then they [the task force] went and hired a vendor that only deals with executives to deal with our [lower-level] employees, most of whom don’t speak English as a first language...what a mistake. We decided we needed to do another RFP.” As implied by this example, personalized services that are misaligned (*i.e.*, directed to the wrong participant cohort) ultimately leads to a misallocation of resources and a potential void in personalization for the targeted group.

When evaluating personalized advice and financial wellness solutions for their plans, some plan sponsors are less concerned with addressing the financial needs of their more affluent executives who are frequently courted and pitched by financial advisors outside of the plan. But the reality is that most DC participants have limited access to high-quality, cost-effective advice solutions outside of their DC plan and instead rely on in-plan financial planning, financial wellness or managed accounts for retirement planning and advice. Data from Cerulli’s 401(k) Participant Survey finds participants who do not work with an advisor most often turn to their workplace retirement plan vendors for retirement planning planning and advice services **(see Exhibit 3)**.

Exhibit 3 | 401(k) Participants: Primary Source of Retirement Planning and Financial Advice, 2023



Source: Cerulli Associates
Analyst Note: Only respondents who do not work with a financial advisor were asked to provide their primary source of retirement planning and advice services. “Other” includes “MBA & economics degree,” “personal investment experience as a banker,” and “my tax accountant.” Percentages do not sum to 100% due to rounding.

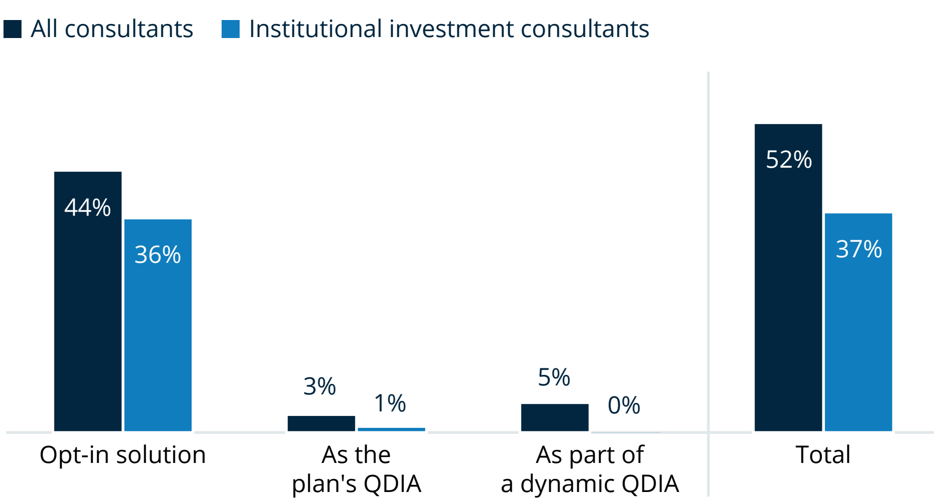
Managed Account Programs

Managed account programs are increasingly prominent within the DC market, with more than half of consultant-intermediated DC plans offering a managed account program **(see Exhibit 4)**. Plan Sponsor Council of America reports 48.8% of plans offered managed accounts in 2022, compared to 36.3% in 2019. As of 2Q 2023, Cerulli finds the top-nine DC managed account programs advise on more than $430 billion in assets. Most large plan sponsors offer or have at least considered offering a managed account investment option. Cerulli survey data shows that plan sponsors most often cite financial planning features and retirement income planning as the most important reason for offering managed accounts, but in conversations with Cerulli, some plan sponsors also cite offering managed accounts to maintain benefits offerings that are competitive with industry peers.

As participants progress through their careers, they tend to accumulate assets and attain more heterogeneous financial profiles and goals. In the years leading up to retirement, participants face the challenges associated with transitioning from the asset accumulation phase of their lives to the decumulation phase, which introduces significant complexity. Affluent participants (*e.g.*, physicians, asset management executives), may appreciate the benefits of DC managed account programs, but many of these individuals tend to have a wealth management relationship with an advisor outside of the plan. Therefore, Cerulli suggests mass-market and middle-market investors (investors with less than $500,000 in household investable assets) and certain mass-affluent investors (with $500,000 to $2 million in household investable assets) approaching retirement are most likely to benefit from a DC managed account program (as opposed to seeking professional advice outside of the plan).

Investors benefit from an in-plan solution for several reasons. First, these programs are considerably less expensive than advice solutions participants could access outside of their DC plan. Second, managed accounts providers are beholden to the Employee Retirement Income Security Act (ERISA) and are subject to a rigorous due diligence process from the plan sponsor and consultant. Third, participants will generally have access to less expensive underlying funds within their DC plan.

Exhibit 4 | Consultant-Intermediated Plans: Managed Account Adoption, 2022



Source: Cerulli Associates

Analyst Note: Data is plan-weighted. All consultants includes insitutional investment consultants and retirement aggregators. Institutional investment consultants are part of major investment and benefits consulting firms. Their services are provided to multiple types of institutional asset owners, including endowments, foundations, and defined benefit (DB) and defined contribution (DC) pension plans. Their parent company is often global and at scale in multiple business lines. Retirement aggregators are registered investment advisor (RIA) firms that have a specialized focus and expertise in advising DC plans. They have a national or regional presence and have grown their AUA by acquiring several local, regional, and/or national retirement plan advisor firms. These firms are increasingly offering wealth management services, often using their retirement plan clients to generate leads.

"Someone from Merrill Lynch is not going to be reaching out to someone with $200,000. But when I look at our workforce, that's a lot of our participants. So, we wanted to bring individualized financial planning and advice for retirement to the mainstream, at a competitive rate... the most immediate need is for our participants for whom retirement is around the corner, but it's also important for our participants to check in on their retirement saving and investing as early as possible."

– *VP, Human Resources, Healthcare Organization*

Overcoming Narrow Perceptions of Managed Account Programs

Many plan sponsors that do not offer managed accounts either do not subscribe to the concept from a cost/benefit standpoint, offer participants financial advice or guidance in another capacity (that they view as sufficient for their participant base), or are considering offering one. Given the looming risk of class-action litigation in the ERISA-covered DC space, fees are understandably important to large plan sponsors and their consultant partners as they consider any investment or plan-level service. Pricing relative to target-date funds often deters them from offering the managed account as the QDIA. However, recent class-action litigation accusing plan sponsors of focusing exclusively on or over-emphasizing fees in their selection process signals that defaulting to the lowest cost option will not necessarily insulate them from litigation and, from a purely regulatory standpoint, is inconsistent with ERISA fiduciary duties of prudence and loyalty.

Based on conversations with plan sponsors, Cerulli suspects many plan sponsors underestimate the value managed account programs can deliver to participants. Specifically, when discussing their perspectives on the value proposition of managed account programs, some plan sponsors compare the investment performance of managed accounts to associated target-date fund vintages. While understanding relative performance is important, it should not be the sole basis for selection of a managed account provider or other retirement provider. When evaluating whether or not to offer a managed account program, plan sponsors should look beyond investment returns and volatility to uncover the full value that these programs deliver to participants.

The ability to speak with an advisor or professional financial planner to help participants make more sound saving, investment, and planning decisions can yield benefits (*e.g.*, more appropriate contribution activity, less "fear-based," harmful trading activity, particularly during times of market volatility) that are somewhat difficult to measure but are, nevertheless, meaningful from a fiduciary standpoint. To be sure, this is less important with regard to purely digital managed account programs, since these programs do not provide participants access to a human advisor but are offered at a lower price point.

Data from Cerulli shows that more than half (52%) of 401(k) participants would prefer to speak to a financial professional over conducting the necessary research themselves or leveraging the advice of other, non-professional connections when making a change to their finance **(see Exhibit 5)**.

We're not convinced that the fees charged by the managed account industry are worth the decisions that they're making, since target-date funds—kind of by definition—are supposed to make all those decisions for you. The managed account providers will, of course, say, 'Well, not everyone is the same investor' and, yes, that's true. But so far, we have not found that the fees charged are worth what we're asking them to do. That's a subjective call, I totally get that."

– *Vice President, Corporate Benefits, Financial Services Company*

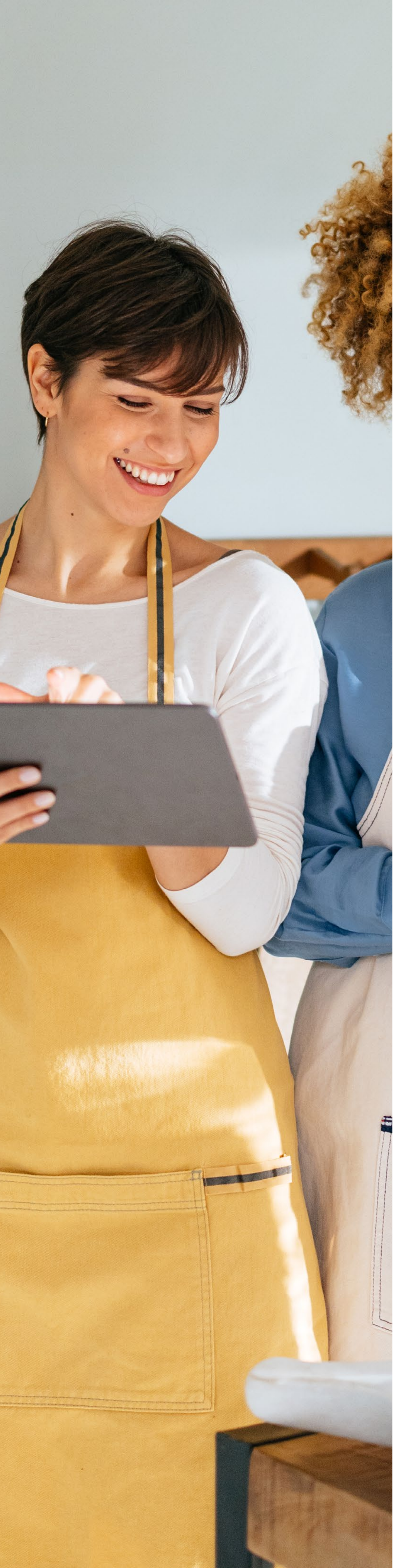
Exhibit 5 | 401(k) Active Participants: Most Likely Action to Make a Financial Change, 2023

Source: Cerulli Associates

Analyst Note: Respondents were asked to select the action they would most likely take if they needed help making a change to their finances.

When you talk to people that use managed accounts, it's usually that they feel more comfortable. In times of stress, they call one of the advisors from our managed account program, who are very well trained, and they [advisors] help people from jumping off the bridge and doing something crazy. You have to think about what that is worth to somebody. It's not about whether you call all the time, it's that one call that keeps you invested and saves you a couple hundred thousand dollars."

– *Director, Actuarial Services, Healthcare Organization*



Driving Participant Engagement

Driving engagement with the managed account program remains a challenge for many plan sponsors and, in conversations with Cerulli, plan sponsors relay varying degrees of success on this front. Some plan sponsors rely on their retirement plan providers or managed account providers to drive and track engagement with their plan and its related services. In some cases, their providers have helped deliver stronger reporting packages that illustrate the impact these engagements have had on participants' financial wellbeing. Harkening back to the non-investment-related benefit of certain managed account programs, plan sponsors should consider infusing this impact reporting into their overall assessments of their managed account provider when evaluating decisions with their investment committees and consultants.

When participants are enrolled in the managed account program, they are more likely to share additional, important data points that can be used to flesh out their financial profile and thereby generate more informed, germane advice and recommendations. Today, managed account programs can extract several participant data points directly from the recordkeepers' platforms, but they still require participants to provide additional information (*e.g.*, assets held outside the plan, spouse/partner's assets) to further tailor their asset allocation and advice.

Managed account participants provide varying levels of data to their managed account provider that can be used to further customize their asset allocation. One plan sponsor notes that while there is strong engagement among managed account participants, other participants are more passive. "On average, we get about three-and-a-half data points of customization [in addition to the data the managed account program is extracting from the recordkeeper]. But we have plenty of people who are enrolled in the managed account program who aren't providing any data—they never interact with it," notes the chief investment officer for a large airline.

Some large plan sponsors tell Cerulli they'd consider sharing additional participant data points with their managed account provider to enhance the value of their solutions. Others with whom Cerulli spoke, however, are skeptical of increased data sharing with vendors due to concerns related to security or aggressive cross-selling, but some express a willingness to do so under the right circumstances or with a trusted provider. While participants would certainly benefit from their managed account provider considering additional demographic data points, this level of personalization would depend on the trust and cybersecurity needed to exchange this data.

"We are very strict when it comes to sharing data, as we should be. But with the right vendor and the third-party risk management review, we would be okay with releasing that type of information [employee demographic data]. We'll be giving similar information on our emergency savings account. And we'll, for the first time, be sharing telephone numbers. To be part of that, you have to do two-factor authentication."

– *Head of Retirement and International Benefits, Grocery Store Chain*

Retirement Income

Most large plan sponsors prefer to keep retiree assets in-plan to attain better scale and negotiating power. About one-third (35%) of plans working with institutional investment consultants actively seek to retain retiree assets, while 40% prefer to retain retiree assets but do not actively encourage participants to stay in plan **(see Exhibit 6)**. Still, many of these same plan sponsors acknowledge it is ultimately the participant's decision and support whatever makes the most sense for their participants. Plan sponsors consistently cite lower investment costs as a primary benefit of keeping retirement assets in the DC plan.

Managed account programs can also be positioned as a retirement income solution for participants nearing, or already living in, retirement. While some plan sponsors don't view their managed account program as a primary retirement income solution for their plan, others articulate the value of having access to relatively low-cost fiduciary advice for near-retirees and retirees within the plan. One plan sponsor discussed a periodic seminar for its employee base, during which the employer explains the various advice options (both in-plan and out-of-plan) available, highlighting the lower cost structure of the DC managed account relative to advice solutions offered outside of DC plans solutions.

Yet when asked if they offer retirement income products/solutions or the type of retirement income products/solutions they are considering, multiple plan sponsors immediately zeroed in on annuity products, indicating that some plan sponsors conflate "retirement income" with "annuity." Adoption of in-plan annuities remains fairly limited within the corporate DC space, with some plan sponsors telling Cerulli they are waiting for the product landscape "to mature" or see which products other employers begin to adopt before taking action on this front.

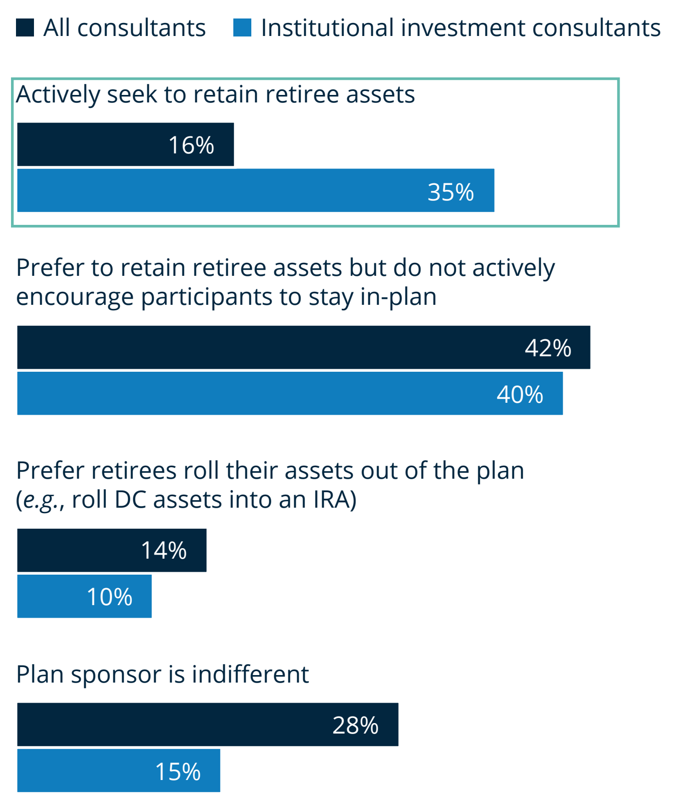
Ideally, personalized decumulation advice and guaranteed income would not be mutually exclusive features of an in-plan retirement income solution. Deciding whether, and how, to invest in an annuity contract is an inherently personal, complicated decision. Therefore, Cerulli asserts managed accounts programs could be a highly effective medium through which to introduce individual annuities within a DC plan. Within a managed account program, participants could work with an advisor to holistically assess their overall long-term spending and savings objectives, which would help to inform whether an annuity would be beneficial and, if so, how much to invest in an annuity contract.

“

We, like many plans over the last five or six years, have made a lot of changes to try and make our plan more of a destination for retirement...What we find is that generally participants are getting into their mid-fifties and they get a local financial advisor who, 100% of the time, is going to tell them 'once you're 59 ½ , roll everything to me for me to manage'... the most important message I communicate to our participants is 'please at least try the managed advice services that we have in our plan because it's going to be less expensive it's going to be overseen by a fiduciary—they have to give advice based on what's best for our employees and that's not always the case if they go outside the plan to a financial advisor."

– *Senior Retirement Plans Administrator, Timber Company*

Exhibit 6 | DC Consultants: Plan Sponsors' Approach to Retaining Retirees Assets, 2022



Source: Cerulli Associates

Analyst Note: Respondents were asked, "Approximately what percentage of your firm's DC plan sponsor clients take the following approaches to retaining retiree assets?" Data is plan-weighted.

Financial Planning and Wellness

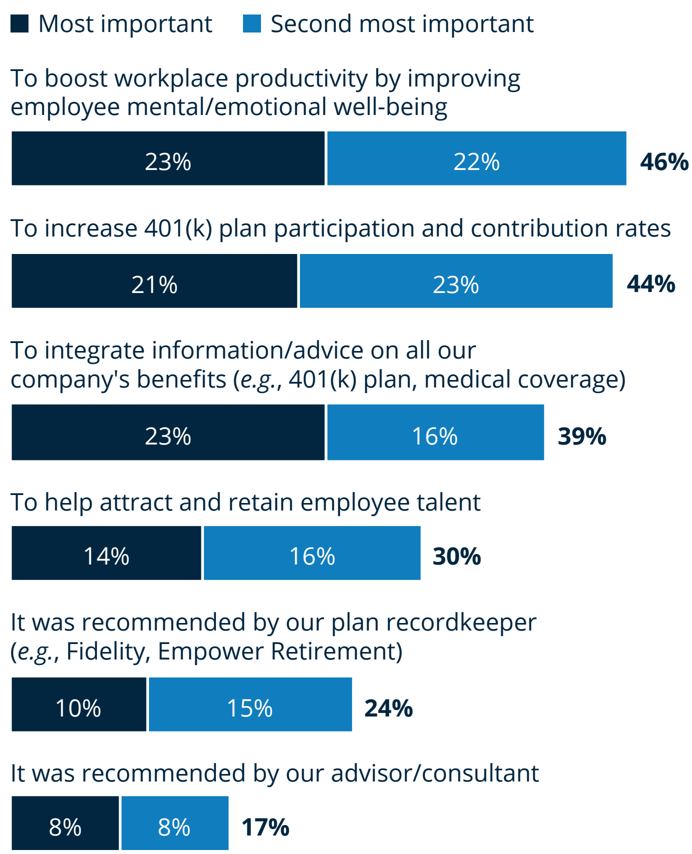
Financial planning is acutely beneficial to investors as they approach retirement, making it a natural service to offer alongside managed accounts. Data from Cerulli's annual 401(k) Participant Survey shows financial planning topics such as Social Security, income planning, taxes, estate planning, and planning for long-term healthcare costs are among the most top-of-mind financial topics for participants in their 50s and 60s. Financial planning can range from one-on-one coaching to building a formal roadmap. While incorporating this service certainly instills elements of personalization into the broader offering, it is more targeted towards participants that are engaged in their finances (or perhaps those who are nearing retirement, as the survey data mentioned would suggest).

The distinction between financial planning and financial wellness can be murky. But, when Cerulli asks plan sponsors to describe what financial wellness means to them, most draw the connection between helping investors make better short-term financial decisions and putting them in a better position to save for the long term. Cerulli defines a financial wellness program as a platform or suite of tools and services designed to help participants more effectively address their short-term financial obligations while promoting superior long-term financial saving behavior. Financial wellness programs aim to provide employees with the foundation of financial knowledge to adequately prepare for retirement. Plan Sponsor Council of America finds only 27% of corporate DC plans offer a comprehensive financial wellness program, beyond a standard 401(k) education program. However, that percentage jumps to 55% when looking at large corporate DC plans, highlighting the relative importance of financial wellness in the large end of the market.

In order to broaden the scope beyond those who are already engaged, plan sponsors should ensure that they have a sound financial wellness program in place. Similar to managed account programs however, driving participant engagement with financial wellness programs is a challenge; in conversations with Cerulli, plan sponsors report only a small percentage of their participants use these solutions. About one-third (32%) of plan sponsors don't offer a financial wellness program because they expect their employees would not take advantage of the program. Periodic campaigns that encourage participants to log into their accounts on a regular cadence (*e.g.*, annually, semi-annually) can help drive engagement, making financial assessments more habitual for participants.

In conversations with Cerulli, multiple plan sponsors highlight the connection between one's financial well-being and their physical and mental health. Taken a step further, participants' physical and mental health can ultimately have implications for productivity, creating a business incentive for employers to ensure that their participants are of sound financial well-being. This sentiment echoes findings from Cerulli's 401(k) Plan Sponsor Survey: nearly half (46%) of plan sponsors cite boosting workplace productivity by improving employee mental/emotional well-being as one of the top reasons for offering a financial wellness program **(see Exhibit 7)**. Following that, 44% of plan sponsors indicate that increasing participation and contribution rates is an important reason to offer these programs, falling under a theme of financial wellness offerings in-and-of themselves being a potential catalyst towards improved engagement.

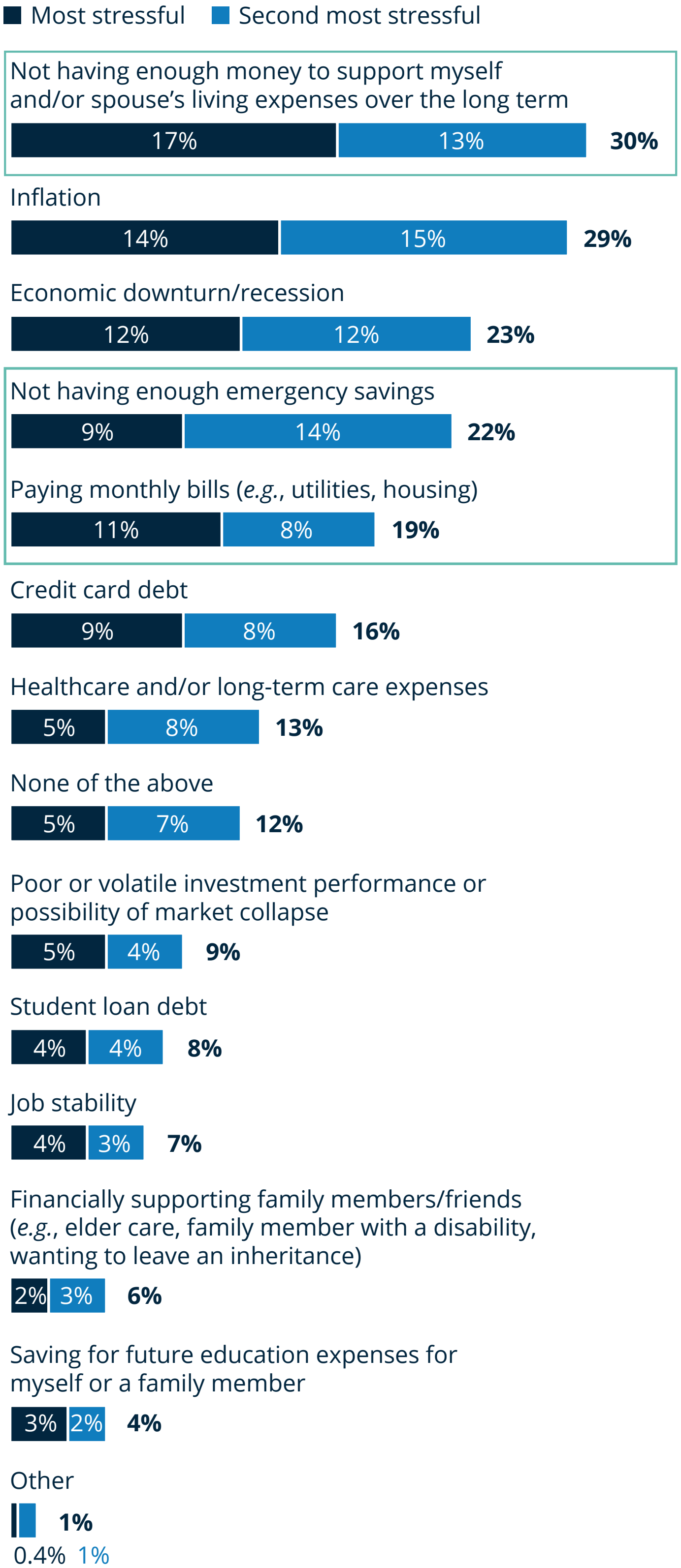
Exhibit 7 | 401(k) Plan Sponsors: Most Important Reasons for Offering a Financial Wellness Program, 2022



Source: Cerulli Associates

Analyst Note: This question was only posed to respondents with a financial wellness program. Respondents were asked to select the most important and second most important reasons. Percentages do not sum to 100% due to rounding.

Exhibit 8 | Active 401(k) Participants: Top Sources of Stress, 2023



Source: Cerulli Associates

Analyst Note: Respondents were asked to select the top-two factors that cause the most financial stress. "Other" includes "health," "housing policy," "Social Security," and "debt." Percentages do not sum to 100% due to rounding.

In terms of features, some plan sponsors express a strong interest in offering support with emergency savings, an aspiration that is likely driven from participant demand – almost one quarter (22%) of active 401(k) participants surveyed by Cerulli cite not having enough emergency savings as a top source of financial stress. While only one plan sponsor with whom Cerulli spoke was looking to roll out an emergency savings account (ESA) for its employees, several plan sponsors emphasized the importance of helping their participants with basic budgeting and short-to-medium-term savings objectives (*e.g.*, buying a house). Notably, Cerulli finds covering ongoing living expenses is a top financial stressor for active 401(k) participants, particularly among Generation Z and Millennial participants **(see Exhibit 8)**.

Multiple plan sponsors also discuss plans to incorporate diversity, equity, and inclusion (DEI) initiatives into their financial wellness offerings. For example, some plan sponsors uncover differences in saving/investing behaviors among different participant demographic groups. A manufacturing firm's treasury executive told Cerulli he is concerned that his company's Spanish-speaking employees are not adequately benefiting from the plan. The goal, in the treasury executive's words, is to make the plan "more inclusive" to ensure plan services and features are benefiting all participants, and not just a subset of the participant base.

Plan sponsors heavily favor one-on-one meetings with a financial advisor or call center representative to help their participants with "next dollar" problems. Still, some components of financial wellness offerings are digital-forward. Cerulli suggests digital financial wellness platforms that offer short, simple participant experiences, with clear, concise action items are most likely to resonate with participants.

The easier, the better. The employer should make it as easy as possible for employees. In one meeting, someone asked, 'what is a target-date fund?' You have to remember that a lot of employees do not understand this stuff. We talk in industry jargon, but you have to put yourself in the employee's shoes. When communicating the reduction in our expense ratio for target-date funds, we included a section with a short video explaining what a target-date fund is."

– Director, U.S. and PR Retirement Plans, Pharmaceutical Company

Performing a Comprehensive Evaluation of Managed Account Programs

At large corporate DC plans, there are usually several internal stakeholders involved in key decisions related to plan design and the investment lineup. These stakeholders are usually executives from human resources, benefits, and treasury, and, in some cases, executives whose primary focus is overseeing their firm's retirement plan offering(s). Often, treasury executives are more focused on the investment lineup, fund performance, and the associated fees, while benefits and HR executives are more focused on plan design and participant communications. Both parties may play a role in evaluating recordkeepers and other vendors, such as managed account providers. In addition, many corporate DC plans utilize a consultant to conduct due diligence on a potential managed account provider. Some plans have a single retirement committee, while others have separate investment committee and retirement plan administration teams.

"HR decides if they want a managed account–that falls through the HR function to decide if we want one. If they decide that we want one, then it gets kicked over to the investment committee to make a recommendation on who we think is the best. We'll do the investment side of the due diligence, we'll make a recommendation, but it's the administrative committee that ultimately has that responsibility [the deciding power]–they own the relationship."

– *Managing Director, Pensions, Airline*

Cerulli finds many plan sponsors employ a fragmented approach to evaluating managed account programs. But since some managed account program providers deliver services that extend beyond algorithmic portfolio management, it becomes imperative for plan sponsors and their consultant partners to evaluate these programs in a holistic, comprehensive manner that assesses the potential qualitative benefits of a program's guidance- and advice-based services in conjunction with the more quantitative investment management side. Access to

financial professionals who are trained to sort through unique financial dilemmas and considerations can have a more substantial impact on participants' long-term financial outcomes than, say, a slight difference in how two programs' investment methodology factors a participant's salary into its asset allocation recommendation.

When addressing participants' financial situations in a holistic manner, financial planning and custom portfolio management are naturally intertwined. This is especially true for near-retirees and those living in retirement whose asset allocation decisions will be significantly impacted by their spending requirements, tax liabilities, Social Security claims, and other financial planning considerations. Managed account programs that can bring all of these services together can offer more informed, and thereby effective, advice for participants. Nonetheless, plan sponsors must be conscious of potential conflicts of interest when evaluating providers, as some providers may use financial guidance and advice interactions as opportunities to cross-sell suboptimal products or services outside of their plan.

Where Investment Methodology Fits into Decision-Making

Large corporate DC plans often work with an investment consultant that will conduct an initial layer of investment due diligence and distill its analysis into a summary for the internal retirement/investment committee. According to data from Cerulli, large 401(k) plan sponsors indicate evaluating service providers is one of the most valuable services offered by their consultant **(see Exhibit 9)**.

> **Investment methodology is not something that would really impact our decision making. It's more of a commodity; they all end up in the same place. It's more about the participant experience and how it is going to help people–that's what the committee wants to know."**
>
> – *Director, Actuarial Services, Healthcare Organization*

Exhibit 9 | Large 401(k) Plan Sponsors: Plan Advisor/Consultants' Most Valuable Services, 2022

Source: Cerulli Associates

Analyst Note: Only respondents partnering with an advisor/consultant were asked about the consultant/advisor's most valuable services. Respondents were asked to select up to three options. Only responses from plan sponsors with at least $250 million in 401(k) plan assets are included.

Typically, when evaluating managed account programs, consultants will solely focus on their investment methodology and performance relative to other managed account programs and target-date fund vintages. Consultants typically act in an investment fiduciary capacity (often in a non-discretionary fiduciary capacity) and harness the knowledge and expertise to perform a rigorous analysis of the various managed account programs in the market. Some ultimately distill an analysis down into very influential "buy," "hold," and "sell" recommendations (or something akin to this), leaving the plan sponsor's investment/retirement committee to make the final decision on which managed account program to offer. "We do a deep dive into managed accounts each year," says one benefits executive. "The consultant gives their benchmarks and their ratings every quarter… our consultant will also compare them to target-date funds."

In conversations with Cerulli, several plan sponsors note concerns about the investment performance of managed account programs relative to target-date funds. However, some plan sponsors relay they put little stock into the different investment methodologies (*e.g.*, forecasting returns by asset class, asset allocation drivers) between managed account providers (even after their consultant conducts and reports its analysis of these investment methodologies).

Cerulli urges plan sponsors not to overlook some of the key intricacies of these programs' investment methodologies. Not only is this important from an ERISA fiduciary perspective, but Cerulli notes the investment methodologies between programs have meaningful differences that impact their suitability for a given plan. For instance, one plan sponsor whose plan has a high percentage of company stock emphasizes the importance of having a managed account program that appropriately factors company stock into asset allocation recommendations.

A Human Touch

As previously discussed, plan sponsors regularly highlight the importance of giving their participants access to a financial professional they can call to discuss their financial situation holistically. Human advisors, as opposed to using a purely digital advice program, are arguably more effective at helping participants address psychological and emotional aspects of saving and investing, particularly during periods of market volatility, such as those experienced at the onset of the COVID-19 pandemic and the first quarter of 2022. Plan sponsors also emphasize the level of trust that is established when working with a financial professional to sort through key financial dilemmas in a holistic, nuanced manner.

"We have a lot of long-tenured people, and they have quite significant balances in our company's stock. Some providers don't manage that as part of their managed accounts; they manage around it. If that's 40% of someone's balance, then they're not getting the full picture. Other providers are incorporating company stock. So, if 60% of their assets are invested in funds the participant selected and 40% is in company stock, that is being accounted for. That is very important to us as the plan sponsor."

– *Benefits Manager, Medical Supplies Organization*

When evaluating managed account providers, it can be difficult to quantify the impact of speaking with a financial professional. Yet the impact of these engagements can be integral to ensuring participants are contributing adequately to their retirement plan and maintain a disciplined, long-term approach to saving and investing for retirement, making this an important feature to evaluate from a fiduciary perspective. When discussing their managed account program within the context of retirement income, one pension executive for an airline company explained that human interaction was among the primary drivers for investor engagement and a vital overarching factor that can bridge engagement to other retirement products, such as annuities.

We already have an annuity window and the usage is below a tenth of a percent... there's every other solution that you can think of and then there is talking to a human being. For us, the human being aspect has the highest net promoter score. I think that's a big reason why our managed account is so well received...I think the human advice component is the primary factor."

– *Mananging Director, Pensions, Airline*

Conflicts of Interest

Perceived conflicts of interest between managed account providers and participants are a major factor when evaluating managed account programs. Many providers use their workplace businesses to expand their relationships with end-investors, capturing a larger portion of wallet share and getting them into more lucrative arrangements.

Recordkeepers offering a proprietary managed account program will, at times, offer plan sponsors steep discounts on recordkeeping administration fees in an attempt to win managed account program placements. However, some plan sponsors are rightfully skeptical of their recordkeepers' motives for offering such steep discounts on either their recordkeeping administration or managed accounts. Plan sponsors should be cognizant of these conflicts of interest and actively address them with managed account providers when they do arise. Ultimately, managed account programs that present less significant conflicts of interest are arguably more likely to act in participants' best interests, resulting in more significant financial outcomes for these participants.

Our managed account provider does not sell anything. They are an unbiased third party. It's not totally clear with some other managed account providers; we know some make money in a lot of different ways."

– *Benefits Manager, Medical Supplies Organization*

Conflicts of interest are top-of-mind for nearly all plan sponsors who spoke with Cerulli. Many plan sponsors also limit the services or types of topics their recordkeepers can have with their participants or create scripts for their recordkeepers' call center representatives to mitigate the risk of inappropriate cross-selling. "We've got a lot of controls and scripts we give to our recordkeeper telling them what they can, and cannot, say to our participants," says one plan sponsor. Still, while turning certain services "off" or creating custom call scripts might mitigate inappropriate cross-selling, it will likely not eliminate it. Moreover, continuously monitoring and constricting vendor behavior adds another time-consuming responsibility to benefits and HR executives who have numerous other important responsibilities and priorities.

The Power of One Advice Expert

From a vendor management standpoint, some plan sponsors tell Cerulli there is value in the simplicity (for plan sponsors and participants) of working with a vendor who can deliver a broader range of personalized advice—from financial wellness to managed accounts. When asked about the vendors her plan uses to deliver financial wellness, planning, and managed account services, one benefits executive from a manufacturing company relates, "Most employers are dealing with a lot of vendor partners as it is. Having a lot of different vendors try to interact with your 401(k) plan gets muddy. It's easier to have it all in one place." Separately, when asked about the services her plan offers participants who are nearing retirement, a benefits manager from a medical supplies company notes, "We're struggling all over because we have all these vendors, so we're telling our participants 'Go here for this service, go here for that service.' I think it can be overwhelming for our participants." As such, providers that can deliver financial advice on a wider range of topics across a larger portion of the participant base may deliver simpler participant experiences and make the lives of benefits and HR executives easier.

Conclusion

DC plan sponsors must evaluate the specific features and services offered across the spectrum of personalized financial solutions—including financial wellness, financial planning and managed account programs. From a fiduciary perspective, plan sponsors should conduct holistic, comprehensive due diligence on managed account programs assesses the value these programs might deliver above and beyond their investment methodology. One-on-one advice sessions with a trusted financial professional can have meaningful impacts on participants' long-term financial outcomes that should not be overlooked and should be considered in conjunction with the investment-related features of the program. Lastly, when evaluating providers' managed account programs, plan sponsors must be cognizant of perceived conflicts of interest and, where appropriate, proactively address any concerns with their current provider or during the RFP process.

Cerulli Research and Consulting

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