Participant Plan Transfers and Account Consolidation for the Advancement of Lifetime Plan Participation

Testimony Before the ERISA Advisory Council

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NARPP The National Association of Retirement Plan Participants

BRT BOSTON RESEARCH TECHNOLOGIES

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Current State

The Evolving U.S. Workforce

- The average worker will change jobs 10 times during his or her work-life (EBRI).
- The U.S. workforce is highly mobile and evolving into a gig economy.
- Intuit Report:
    - In the U.S. alone, contingent workers will exceed 40 percent of the workforce by 2020.
    - Traditional full-time, full-benefit jobs will be harder to find.
    - Self-employment, personal and micro business numbers will increase.
- Traditional retirement systems need to evolve with the workforce– to be more inclusive of non-employer-based systems with universal portability.

The U.S. Retirement System is One-Fifth Complete

- DC system is a highly efficient mechanism for getting employees' assets into the plans.
- The parts of the job not completed are:
  - Universal access for workers outside the traditional employer/employee relationship (Gig workers)
  - Frictionless portability
  - Retirement income/decumulation systems
  - Behaviorally-affective communications programs for a voluntary saving system *(How many people would continue Social Security deductions if it were voluntary?)*

The Journey to Retirement Readiness is Epic

Laurie Rowley, President of NARRP:

“Keep in mind the magnitude of what we are asking workers to do: Save enough in their working years to fund 35 years of living after they stop producing income.”

David Sinclair, Co-Director of a lab on aging at Harvard Medical School:

“Over the last ten years, my lab and many others around the world have shown that it’s not just possible to delay aging, but to reverse aspects of it. The first person to live to 150 has already been born. And it’s not crazy to say that anymore, it used to be, 10 years ago.”

A New Stage of Life: Elderhood

Laurie Rowley, President of NARPP:

"Americans are living longer than ever before, and that means for many people, that their post-income producing era will extend 30 or 40 years.

And while retirement has come to be associated with a time for pursuing hobbies, interests, travel, and encore careers, these activities more accurately define the early years of retirement: ages 65-75.

But we know that many people are living well beyond 75—and that phase of life will be distinctly different from the early, post-income-producing years. We call this latter phase in life 'Elderhood'.

Elderhood is distinctly different from the early years of retirement: the pace of life changes and people will want and need more security and support. Careers are a distinct but distant memory.

By defining this phase of life, we can help people plan for it so that when they enter Elderhood, their final stage of life, they can do so with the satisfaction of a life well lived."

The Big Picture of Life

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Access is Not the Biggest Problem

Access, while still a challenge, is not the biggest challenge to post-income-producing financial readiness.

- State initiatives will create more mechanisms for access but they will have even greater weaknesses than what DC systems face today.
  - Lower portability due to a Roth IRA structure will create many small-balance accounts that are in the red-zone for probability of cashing out
  - No match, which reduces motivation to save
  - No education, guidance and encouragement from the employer
  - Still requires an employee/employer relationship
- The DC system is not yet completed when it comes to making funds mobile between accounts at different employers.
- To optimize the impact of the DC system on retirement readiness the goal is to reduce the friction of money movement to the same level as the US banking system.

The Face of Friction

A Quick Review of RCH/BRT Study Findings

- In May of 2015, I presented findings from a large DC participant study done under the auspices and collaboration with Retirement Clearinghouse (RCH). This study addressed the behavioral and mechanical influences on lifetime-participation decision-making.
- The study focused on what participants do with existing DC accounts at job change - particularly why people leave (at least partially and temporarily) the retirement savings system (leakage) in the form of cash-outs.

Why Are There So Many Cash-Outs?

Cashing out is not a natural proclivity, in a real sense we have created much of it:

- Very few (4%) of those who cash out say that would have been their anticipated action before a job change occurred.
- The vast majority who cashed out agree DC balances should only be used strictly for retirement.
- Regret persists among half who cashed-out.

Penalties– A Weak Deterrent

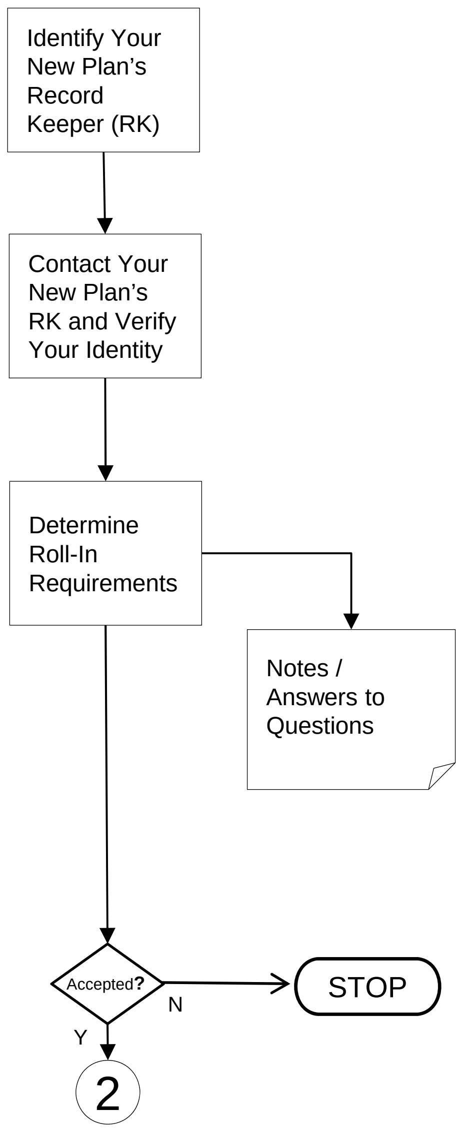
- Eight-in-ten "say" they were aware there were penalties and taxes due if they cashed out ….and did it anyway.
- Prospect Theory is likely in play: The sense of "loss" is not sufficient to stop the cash-out.
  - It may not be perceived as a "loss" at all, but rather a gain of purchasing power.
  - The money will come out of the DC account often funded by employers' contributions ("I get my money out, the match paid the penalties and taxes").
  - This money has already been removed from the participant's cash flow. The pain of loss has subsided.
  - No sensitivity over an arc of prices tested to have the process done for them.

Poor Portability Is A Big Problem

- Of the four primary options a participant has regarding their DC account when they change jobs, the most desirable one is the most difficult and complicated to accomplish.
- **The least desirable is the easiest.**
- **The most desirable (arguably) is the hardest.**
- Rolling into one's new employer's DC plan is by far the hardest of the four options.

What Friction Looks Like
The Process of Moving Plan to Plan

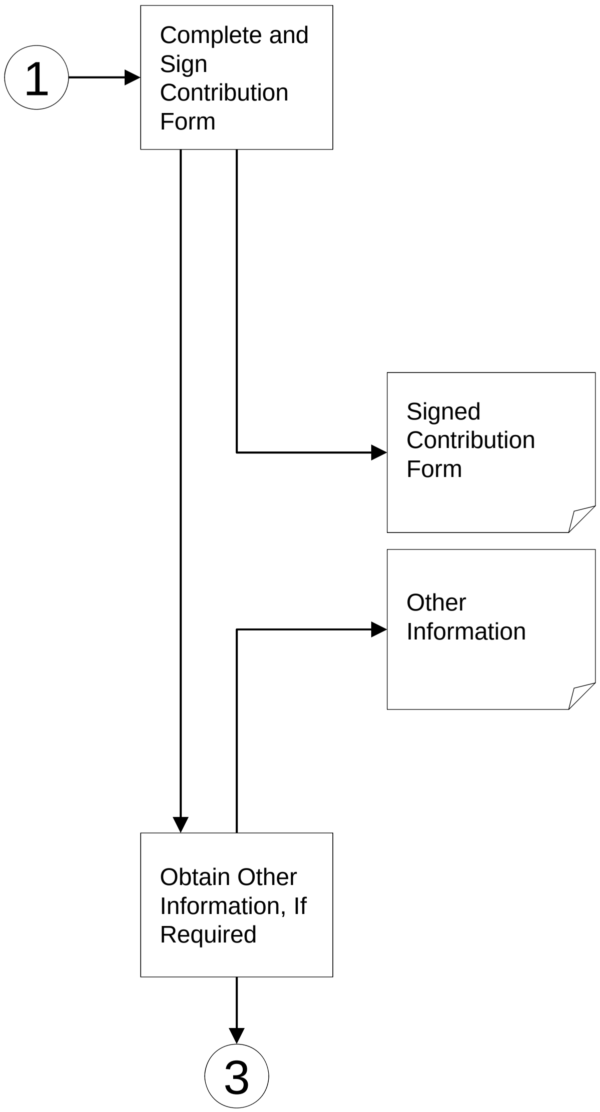
Step 1: Determine Eligibility to Roll-Into New Plan



Step #1 Tasks

1. Identify your new employer's plan record-keeper (from statements, etc.)
2. Gather your personal information (name, SSN, employer, account number, PIN, etc.)
3. Contact your new employer's plan record-keeper
4. Determine the requirements & eligibility for rolling your old plan account into the new plan
   - <u>Ask the following questions:</u>
   - i. Will you accept my old plan account?
   - ii. Do I need a contribution form?
   - iii. How can that form be delivered to me? - e-mail, fax, mail
   - iv. Are any signatures other than my own needed on the form? If so, whose?
   - v. When sending the form back – do you need my "original" signature, or can I fax/e-mail the form back?
   - vi. How should the check be made payable? (this needs to be very specific or it may be rejected by your new plan)
   - vii. What other documents do you require to accept my roll-in?
     - a. Distribution statement from my rollover check, i.e. 401(k)/ IRA statement
     - b. Letter of Determination from old plan
     - c. Letter from prior plan administrator "qualifying" the plan
     - d. Other?
5. If your account is not eligible for roll-in, STOP
6. If your former account is eligible for rolling into your new plan, proceed to Step #2

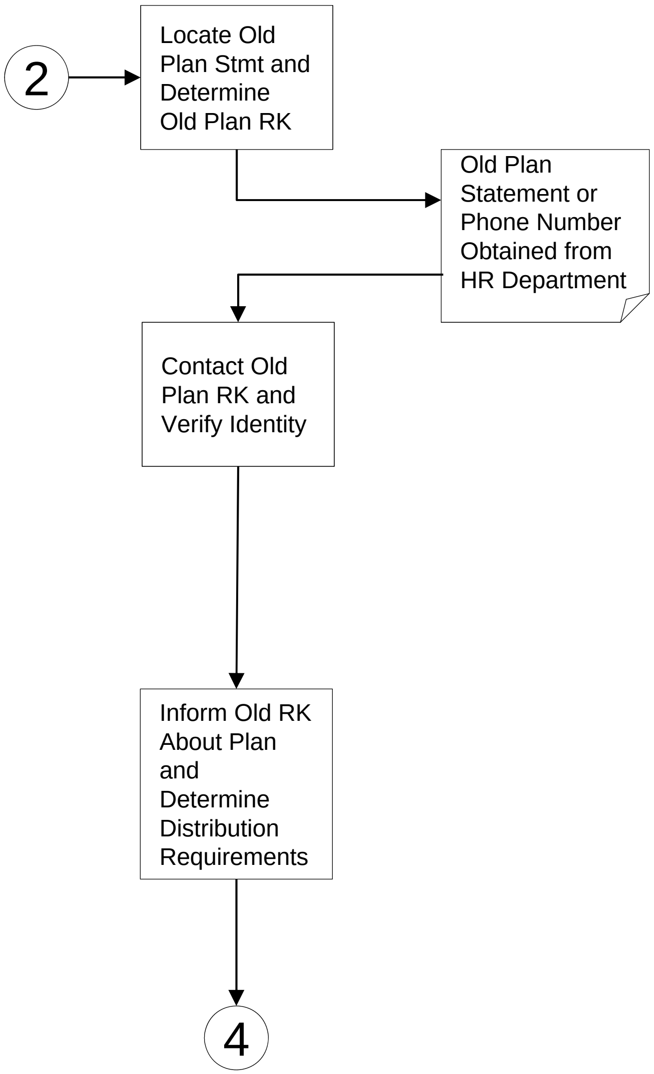
Step 2: Complete Forms to Roll-Into New Plan



Step #2 Tasks

1. Complete and sign the new plan's Contribution Form
   - 4 basic pieces of information needed for the Form
     - i. Personal Information
     - ii. Prior plan information, i.e. name of plan, EIN, type of plan
     - iii. Investment selections
     - iv. All required signatures
       - a. Prior plan administrator
       - b. Other?
2. Gather other required documents from Step 1.3.vii
3. Proceed to Step #3

Step #3: Determine Requirements to Roll Out of Old Employer Plan



<u>Step #3 Tasks</u>

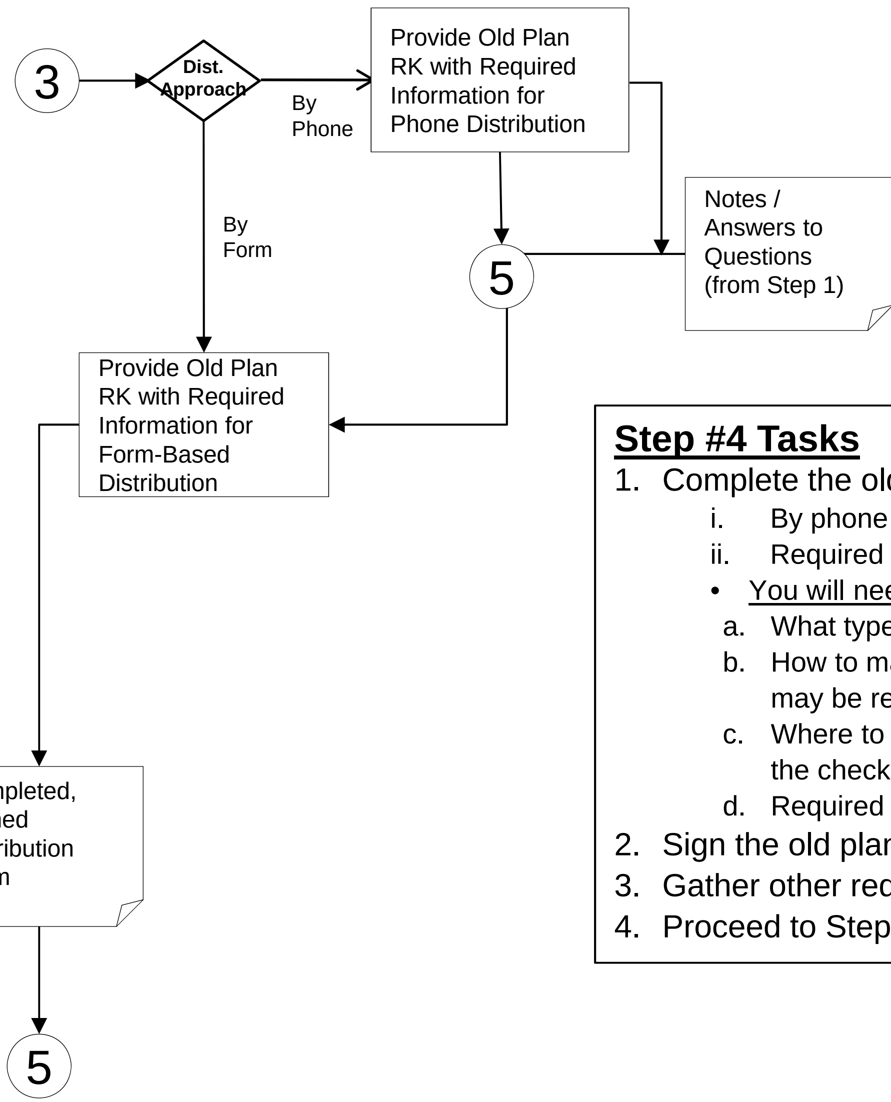
1. Identify your old employer's plan record-keeper
2. Gather your personal information (name, SSN, employer, account number, PIN, etc.)
3. Contact your old employer's plan record-keeper
4. Determine the requirements for rolling your account out of the old plan
   - <u>Ask the following questions:</u>

   i. How can the plan be distributed?
      a. Phone
      b. Forms
      c. Electronically – internet

   ii. Are there any other documents that are required to complete the rollover? e.g., a Letter of Acceptance or Signature Guarantee

   iii. If by form – ask if one or more "original" signature is needed
5. Proceed to Step #4

Step #4: Complete Forms to Roll Out of Old Plan



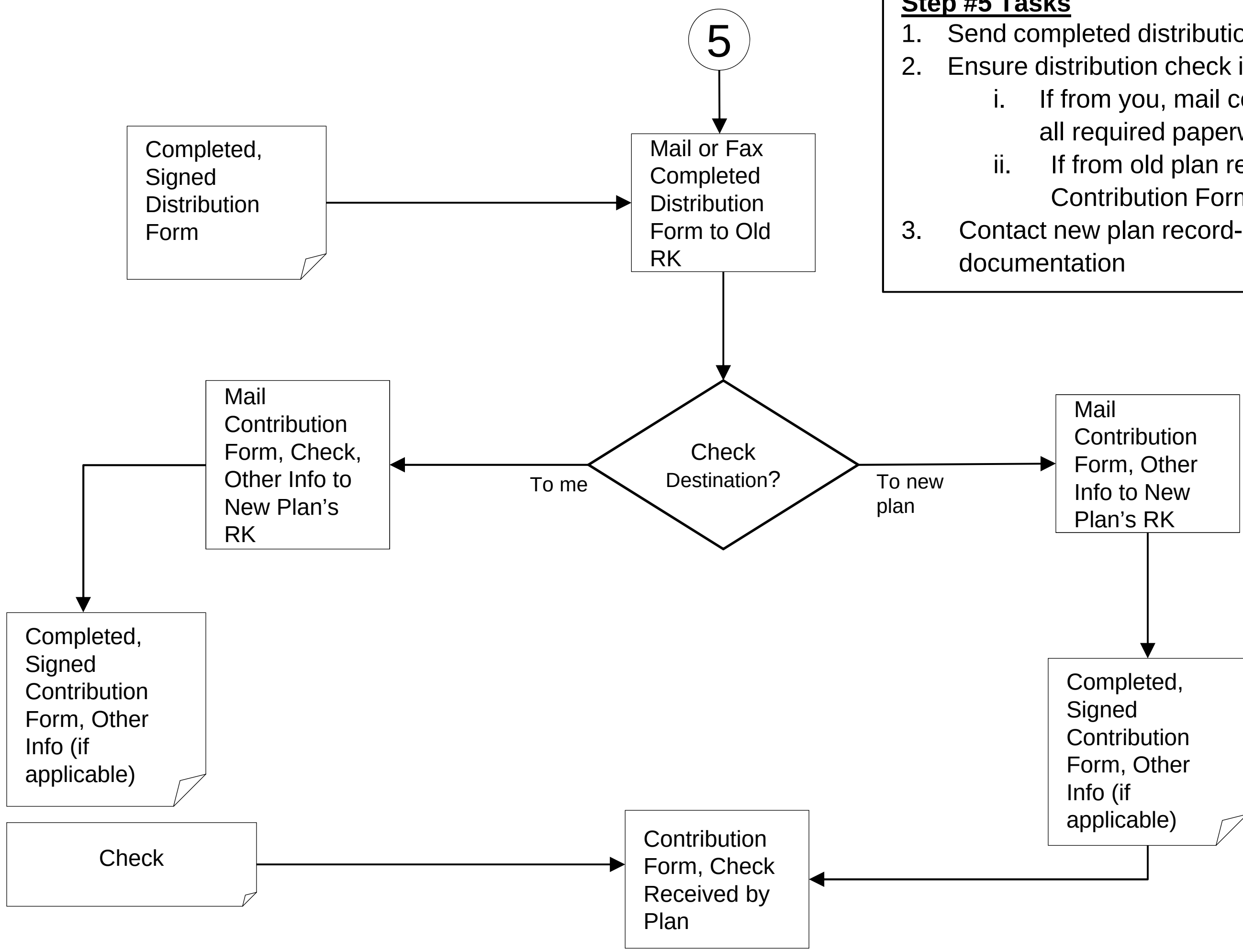
<u>Step #4 Tasks</u>

1. Complete the old plan's record-keeper with distribution information
    - i. By phone
    - ii. Required form
    - • <u>You will need the following information:</u>
        - a. What type of new plan you have – 401(k), 403(b) etc.
        - b. How to make the check payable? (this needs to be very specific or it may be rejected by your new plan)
        - c. Where to send the check (if applicable – some institutions will send the check only to you at your address of record)
        - d. Required signatures (you and/or spouse, plan administrator)
2. Sign the old plan's distribution form
3. Gather other required documents from Step #3.3.ii
4. Proceed to Step #5

Step #5: Send All Forms, Required Documentation & Check to New Plan

Step #5 Tasks

1. Send completed distribution form to old plan record-keeper
2. Ensure distribution check is sent to your new plan's record-keeper
   i. If from you, mail completed Contribution Form, check and all required paperwork
   ii. If from old plan record-keeper, mail completed Contribution Form and all required paperwork
3. Contact new plan record-keeper to verify receipt of all required documentation



Transaction Type: Small Balance (<$5,000) Cash-Out

Step1: Do Nothing

Step 2: Deposit the Check

Transaction Type: Large Balance Cash-Out

Step1: Click

Step 2: Deposit the Check

Transaction Type: Create an Orphaned Account

Step1: Do Nothing

Step 2: (see step 1)

Barriers to Engagement

Automatic Features Alone Are Not Enough

- Simply enrolling people in a plan does not address the biggest challenge to lifetime “participation”.
- In fact, it may be causing part of the problem with retirement saving.
- There is a difference between “Enrollees” and “Participants”.
- Ease of enrollment does not necessarily engage a person with retirement saving.
- State-level initiatives will increase access and get many people physically in the “plan” but not necessarily “emotionally” in the plan.
- Default rates are not set based on adequacy but rather least likely to cause an opt.
- Many participants confuse the two and mistake default rates as the recommended amount.

After Ten Years of the PPA…

Vanguard's Annual Study "How America Saves" Shows:

- In 2015 dollars, the median DC account balance has actually dropped since 2006 from $30.5K to $26.4K.
- Implicitly, automatic enrollment without mandatory auto-deferral increase is creating a large number of small accounts.
- "Build it and they will come" works for baseball but doesn't necessarily work in the retirement savings arena.
- External motivators are needed to drive people into the mechanisms for retirement saving, and keep them there.

Product Innovation Requires Behavioral Solutions

- National Association of Retirement Plan Participants (NARPP) conducted a study to define, measure and determine the drivers of “Engagement”.
- 2016 On-line survey of 5,000 active DC participants.
- NARPP’s analysis identified factors that lead to higher engagement (i.e., interaction with the recordkeeper and reaching for retirement readiness).
- **Increasing engagement is within the control of the recordkeeper and, by extension, the plan sponsor.**

Engagement Without Trust is Very Difficult

- The study also proved that trust in the employer and recordkeeper is foundational to a variety of positive participant behaviors such as elevating deferral rates and engagement.
- The question becomes how do you build trust?
- **Communication style with the participant is the most important factor for building trust.**

Building Trust

Below are the most powerful drivers of trust, listed in order of magnitude.

- The single-most powerful driver of recordkeeper trust (4 times stronger than the second most powerful driver) is presenting information to participants in a way that is perceived as being in their best interests.
- Maintaining a positive message (i.e. messages that avoid fearful or negative tones) is essential.
- Information such as low projections of retirement replacement ratios and high probability of running out of money erode trust.

2015 Collaborative study by BRT and EBRI on which was more effective in raising deferral rates: projections of retirement replacement ratios or high probability of running out of money.

Conclusion: Neither but probability of not running out of money is more effective*.*

Building Trust (continued)

- Presenting fee information in a way that is easy to understand.
- Feeling comfortable and competent with financial planning for the future. (Financial literacy is much less motivating than subjective self-perception of financial competence.) (Dunning-Krueger Effect)
- Recordkeeper trust has the potential to be lowered by materials containing complicated financial language. When participants don't understand what is being said to them (particularly when trying get them to voluntarily reduce their seemingly already scarce take-home pay), trust plummets.
- Importantly, participants want to feel in control of the retirement savings process. To participants, being in control does not require high levels of financial literacy or excessive information and data.

Increasing Engagement

Building engagement is critical to life-long participation.

The factors that increase engagement:

- Positive motivation to prepare for retirement (scare tactics don't work)
- Creating a belief that retirement readiness can be achieved
- Empowering the participant with a sense that it is possible to be in control of outcomes and the process
- Providing a vision of what success looks like
- Perceived level of financial knowledge (the more you believe you know the more engaged you become)
- Communications materials that motivate participants to take action
- Knowing how to estimate the amount of money one will need to accumulate to retire (if they have clear goals, they are more engaged in meeting them)

Increasing Engagement

The factors that increase engagement: (continued)

- A feeling that one understands investing principles
- A sense of financial stress (acting as a motivator)
- A social structure that makes one feel one can take some risks (Financial Courage)
- A healthy appreciation that the future is uncertain
- A belief that retirement readiness will be achieved

Question: Does a mandated or auto-enrollment plan with no match create engagement in the employer?

Proven Behaviorally-Based Solutions

Developing Behavior Changing Communications

By combining principles of behavioral finance with intuitive design NARPP has developed a communications system that has proven to be effective at increase engagement with plan participants.

Case Study:

In partnership with a large state 457 plan NARPP implemented this system in just six months we had the following results:

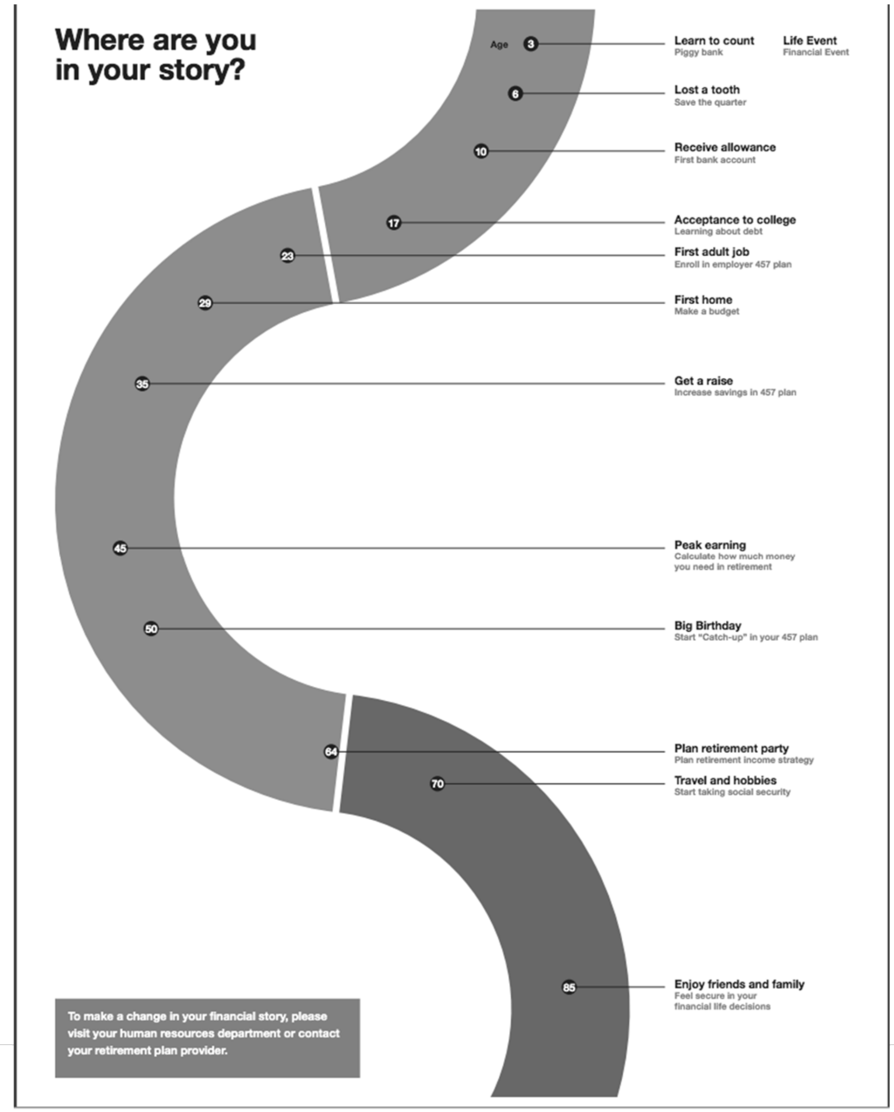
- Increased plan participation by 25%
- Increased use of auto-escalation by 600%

Case Study: NAGDCA NSRW Campaign

The objectives of the National Save for Retirement campaign are to:

- Build trust and confidence with participants
- Increase participants' level of financial courage (a requisite for increasing savings rates)
- Shift the participants to "implemental mindset"

Case Study: NAGDCA Campaign

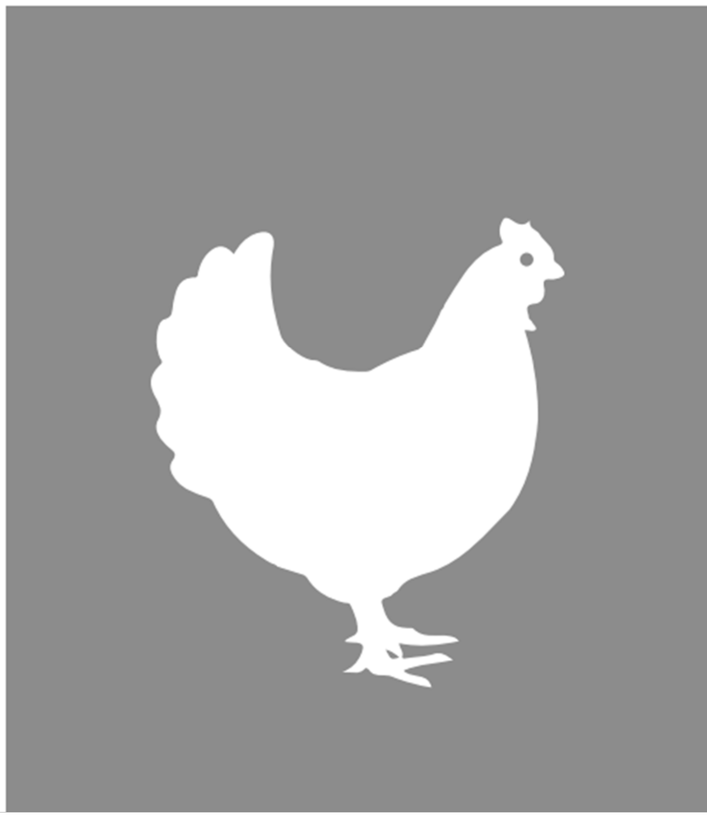


Case Study: NAGDCA Campaign

Retirement Journey Field Note #1

Start As Soon As Possible

YOUR WHOLE STORY



One of the smartest things you can do on the way to retirement is to start saving as soon as you are able to.

It only takes about 10 minutes to join your company's retirement savings plan. For more information on how to join, contact human resources. If you are not able to save more today, make a budget or a plan to start when you can.

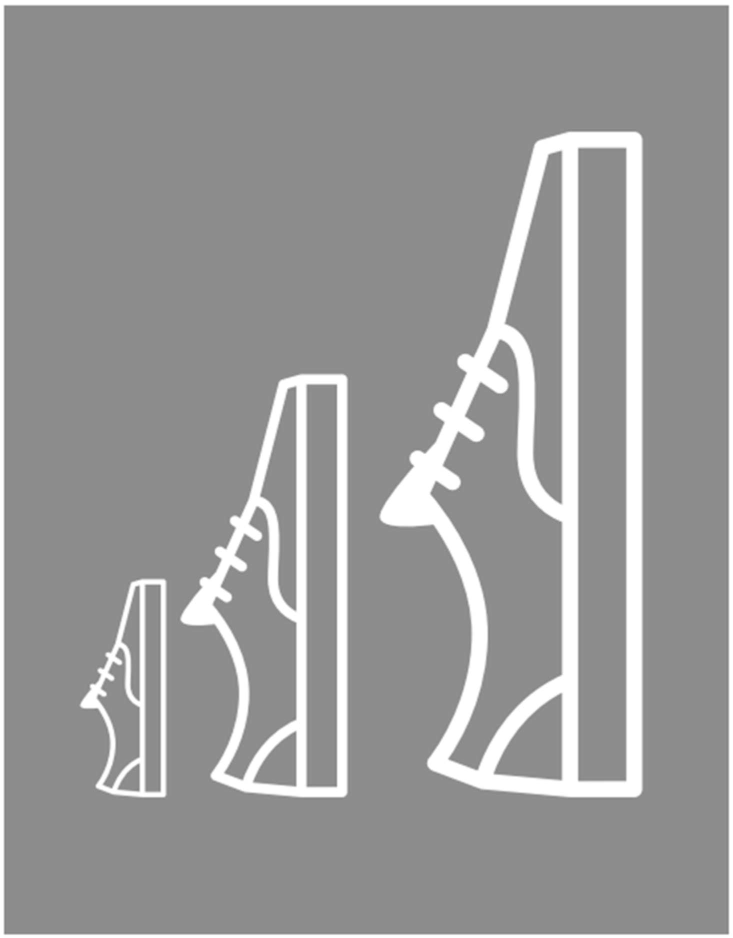
This illustration is a hypothetical compounding example that assumes a $50,000 salary and biweekly salary deferrals (for 30 years) at a 6% annual effective rate of return. It illustrates the principle of time and compounding. This chart is for illustrative purposes only and is not intended to represent the performance of any specific investment. Actual returns will vary and principal value will fluctuate. Taxes are due when money is withdrawn.

Case Study: NAGDCA Campaign

Retirement Journey Field Note #8

One Small Step Today…

YOUR WHOLE STORY



…goes a long way for your financial future. Make sure the amount you're saving keeps up with you during your working years.

Experts recommend contributing at least 10% of your current income to your future retirement. To increase your contribution contact your plan provider. If you are not able to save more today, make a budget or a plan to start when you can.

Conclusions

Conclusions

- Lifetime plan participation does not necessarily happen with automaticity and mandates.
- There are enrollees and there are participants.
- Engagement continues to be the source of frustration among plan sponsors and providers.
- With engagement we will dramatically improve outcomes.
- There is a well-defined path to better engagement.
- There are no short-cuts to better outcomes…we have to step back and create the foundation of trust upon which we will get true lifetime plan participation.

Addendum

About the RCH/BRT Study

Methodology:

- 5,000 active DC participants
- On-line data collection
- SSI Respondent Panel
- Survey conducted from April 13 – April 24, 2015
- Weighted by geography, age, gender, and RK