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WASHINGTON DC | NOVEMBER 2–5, 2014

ORIGINAL>ESSENTIAL>UNBIASED>**INFORMATION**

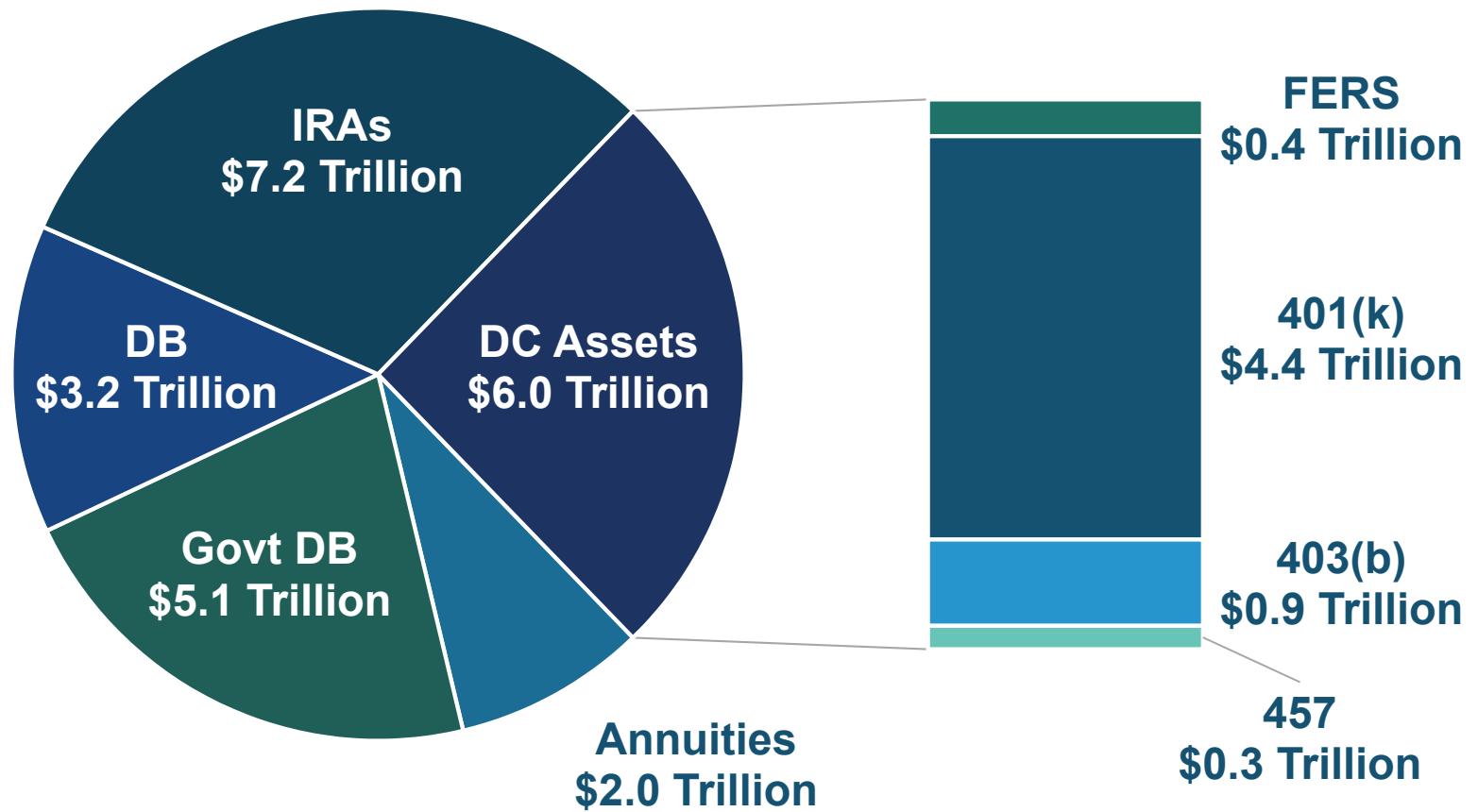


## Managed Accounts in 401(k) Plans: Solution or Fad

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# US Retirement Assets

36% of US Household Financial Assets



Source: Investment Company Institute (ICI) AS OF 6/30/2014

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# DC Plan Investment Management Solutions

## Managed Accounts

Participants delegate custom asset allocation and rebalancing decisions to investment professionals using the Plan's fund line-up

## Target Date Funds

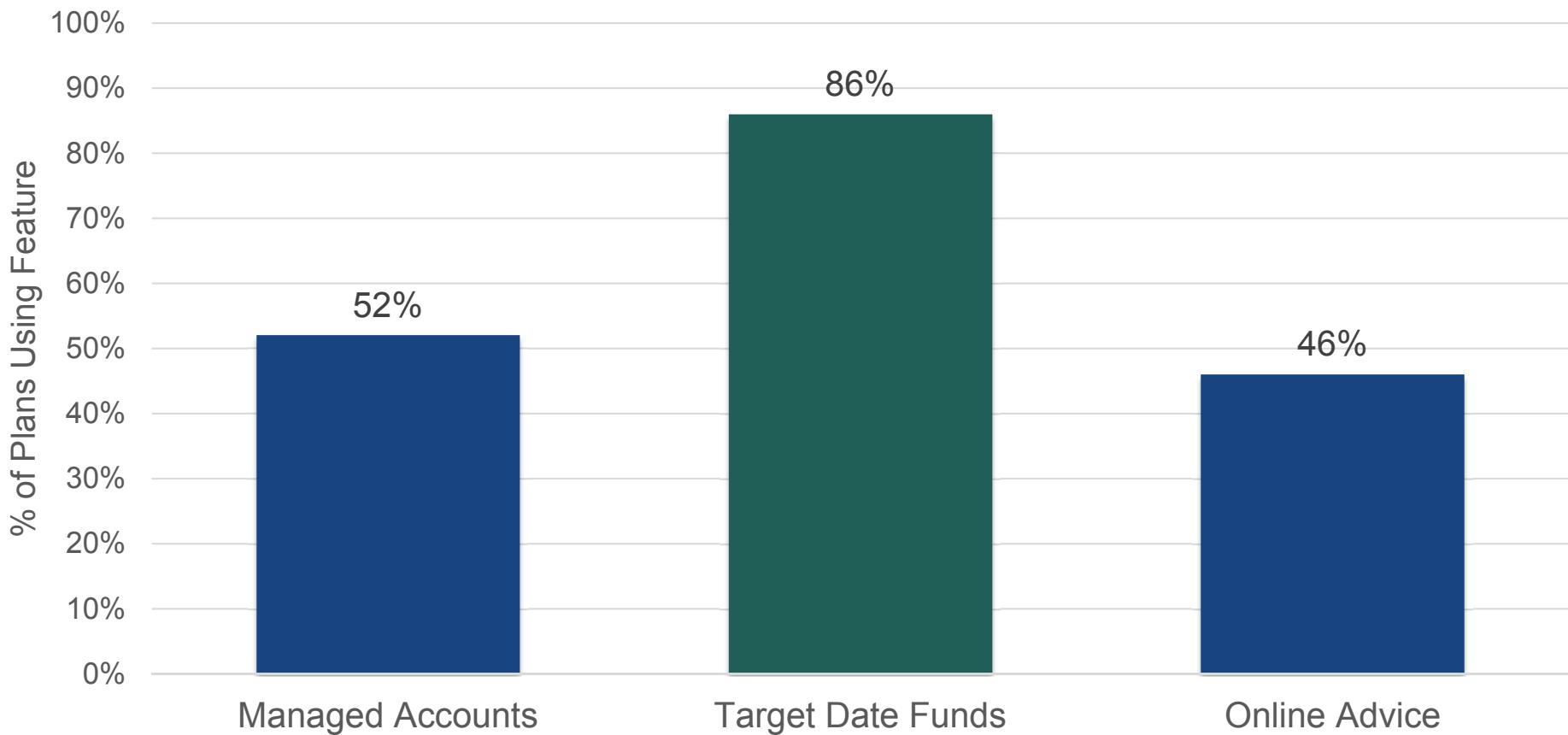
Participants select pre-mixed asset allocation fund based on retirement year

## Online Advice

Participants use website advice tool to make their own decisions



# DC Plan Usage Investment Management Solutions



Source: Survey of Aon Hewitt's recordkeeping clients "2013 Trends & Experience Defined Contribution Plans"



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# DC Plan Usage Target Date Funds

- Most commonly used asset allocation solution
- 88% of participants <25 years old
- 68% of participants 25-35 years old
- Participants average 38 years old
- Average account balances \$16,000



Source: "Help in Defined Contribution Plans" Survey published May, 2014 by Financial Engines / Aon Hewitt

# DC Plan Usage Managed Accounts

- Second most used asset allocation solution
- 54% of participants >55 years old
- Average age 48 years old
- Average account balance \$93,000
- Highest usage by participants with account balances \$50,000 – \$250,000



Source: "Help in Defined Contribution Plans" Survey published May, 2014 by Financial Engines / Aon Hewitt



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# DC Plan Usage On-Line Advice

- Participant responsible for rebalancing
- Popular for participants with >\$250,000 balances
- Average account balances \$155,000
- Average age 45 years old



Source: "Help in Defined Contribution Plans" Survey published May, 2014 by Financial Engines / Aon Hewitt



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# Plan Feature Usage by Age

- Young participants tend to use target date funds
- Managed accounts increases for participants >45 years of age

Age Range	Target Date Funds	Managed Accounts	Online Advice
< 25	88%	6%	6%
25-35	68%	20%	12%
35-45	47%	35%	18%
45-55	36%	45%	19%
> 55	28%	54%	18%

Source: "Help in Defined Contribution Plans" Survey published May, 2014 by Financial Engines / Aon Hewitt



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# Plan Feature Usage by Balance

- Participants with lower account balances use TDF
- Participants with higher account balances use managed accounts and online advice

Account Balance	Target Date Funds	Managed Accounts	Online Advice
< \$5,000	86%	8%	6%
\$5,000 - \$15,000	61%	30%	9%
\$15,000 - \$50,000	35%	50%	15%
\$50,000 - \$100,000	17%	61%	22%
\$100,000-\$250,000	9%	60%	31%
> \$250,000	6%	47%	47%

Source: "Help in Defined Contribution Plans" Survey published May, 2014 by Financial Engines / Aon Hewitt



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# 404(c) Status Managed Accounts

- Plan fiduciaries preserve 404(c) status if participant:
  - Exercises control over the plan account
  - Retains the power to open and close its managed account – hire and fire



# 404(c) Status Managed Accounts

- Plan fiduciaries' limited liability
  - DOL 404(c) (d) (2)(ii) and (iii)
  - May not be directly responsible for the investment manager acts and omissions

*Plan sponsor still has fiduciary responsibility*

- For selection and monitoring of the investment manager



# Due Diligence Managed Accounts

- **DC Plan Investment Policy Statement**
  - Should provide for Managed Accounts
  - Criteria for selection and monitoring
- **Qualifications of the investment manager**
  - SEC-registered investment advisor
  - Proven performance record
  - ERISA 3(38) fiduciary status
  - Asset allocation methodology
  - Reporting
- **Monitor Performance**



# Due Diligence Managed Accounts

- **Reasonableness of the fees**
  - Plan sponsor responsible to negotiate, monitor fees
- **Typically asset-based fees**
  - With break point reductions as assets grow
  - At participant asset level
  - Plan enrollment tiers
- **Fees typically deducted from the participant's account**
  - Monthly or quarterly
  - In arrears



# GAO Report Managed Accounts

*“401(k) Plans, Improvements Can be Made to  
Better Protect Participants in Managed Accounts”*

- Examined top 8 providers
  - 95% of 401(k) market
- Fiduciary status varies if participants opt-in
- Limited participant information
  - Fee, performance and benchmark
- Challenging for plan sponsors to evaluate/monitor



Source: GAO-14-310: Published: Jun 25, 2014. Publicly Released: Jul 29, 2014



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# GAO Report Managed Accounts

- Recommendation:
  - Fiduciary status/requirement
  - Address conflicts of interest
  - Greater disclosure on fees, performance, benchmarking
  - Evaluation guidance for plan sponsors
  - Standardized performance and benchmark information
- *Expect DOL guidance or regulatory action*



Source: GAO-14-310: Published: Jun 25, 2014. Publicly Released: Jul 29, 2014



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# DOL Guidance

## Field Assistance Bulletin (FAB) 2007-1



- Detailed summary of plan fiduciary's duties
  - Evaluate, select and monitor provider
  - Select ERISA 3(38) fiduciary as investment manager
  - Manage account in participant's best interest
- Plan fiduciary's ongoing responsibilities
  - Monitor changes in the qualifications
  - Adviser complies with contractual obligations
  - Investigate participant complaints about the provider
  - Periodically evaluate services and fees



# Investment Advice to Participants

## DOL Final Rule 2011

- Managed account providers can be affiliated with the record keeper's fund managers
  - Previously required independent, unaffiliated firm
  - Provides exemption to prohibited transaction
  - Requires controls on conflicts of interest



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# Investment Advice to Participants

## DOL Final Rule 2011

- Must be monitored and meet specific conditions
- Use unbiased computer model for asset allocation
  - Written certification that model is unbiased
  - Uses accepted investment theories
  - Meets requirements by an independent expert



# Investment Advice to Participants

## DOL Final Rule 2011

- Managed account provider's compensation
  - Does not favor proprietary, affiliated or high revenue share funds
  - Compensated on a level fee basis
- Must make written fee disclosures to participants
- Third party annual audit and attestation letter



# Investment Advice to Participants

## DOL Final Rule 2011

- Plan sponsor must authorize in a formal contract
  - Advice arrangement
  - Advisor compensation
  - Participant charges
- Plan fiduciary has an established due diligence
  - Considers multiple managed account providers
  - Set qualifications in selection process
  - Monitors provider ongoing



# Typical Factors Used for Advice

- Total Retirement Planning Approach
  - Expected retirement age
  - Social Security benefits
  - Spouse's assets/benefits
  - Income replacement
  - Savings rates
  - Documentation and depletion rates
  - Mortality assumptions



# Conclusion Well-Designed Program

- Independent investment manager
- ERISA 3(38) fiduciary
- Robust research
- Proven asset allocation methodology
- Personalized portfolios include participant's outside assets



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# Conclusion Well-Designed Program

- Participant personal evaluations
- Disclosures
- Ongoing account monitoring and management
- Direct access to investment advisors
- Periodic, accurate statements with performance
- Cancellation without penalty

