

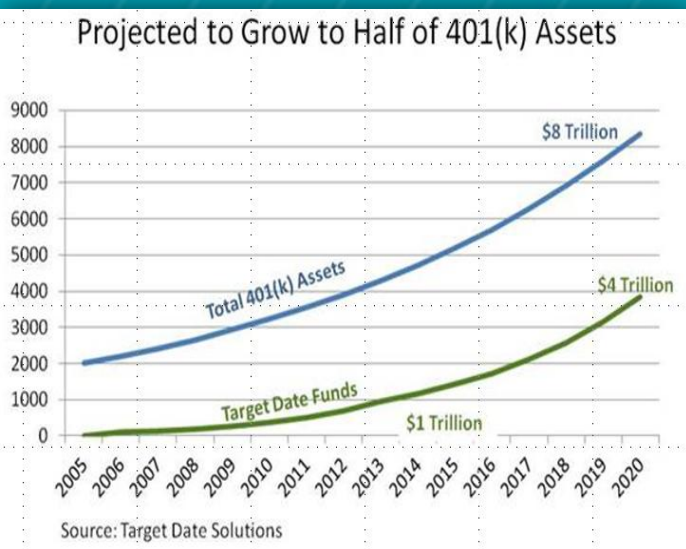
PSCA 2019 NATIONAL CONFERENCE

BUILDING A BETTER RETIREMENT

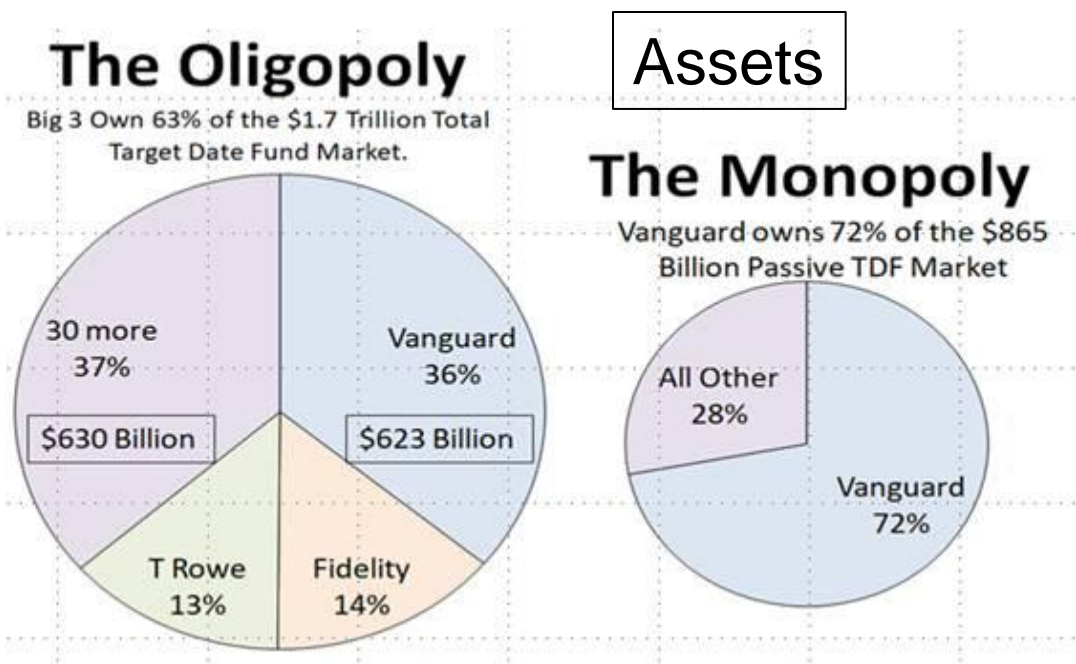


Target Date Funds: should we be satisfied with what we have?

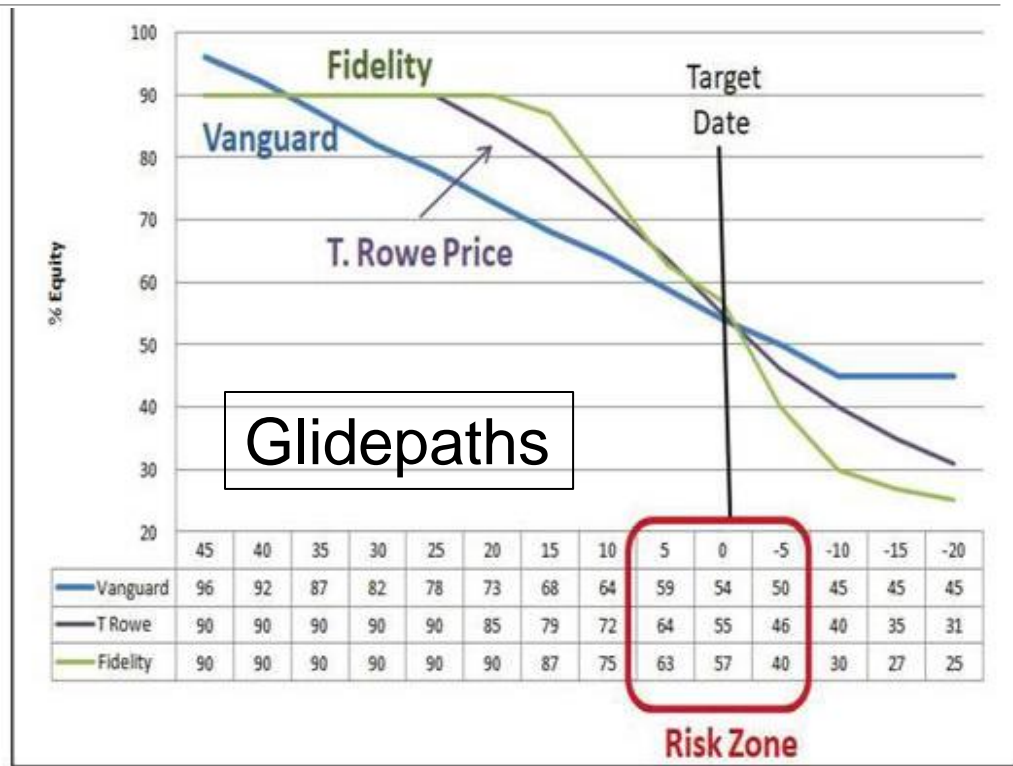
Ronald Surz, President of Target Date Solutions
Neil Lloyd, Partner of Mercer



Today's TDF Marketplace in the U.S.



Source: Sway Research



Source: Target Date Solutions and PIMCO

Does this introduce complacency, the “wisdom of the herd” and potentially stifle default fund innovations?

Personalized Accounts

FORM
— AND —
FUNCTION

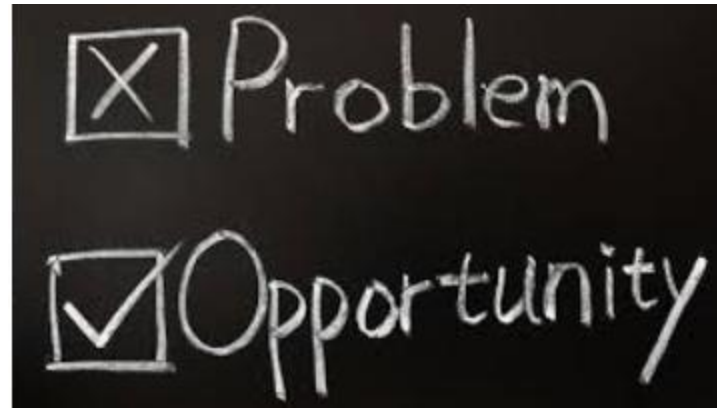
Protection

PSCA Mission:

Solve real problems, create positive change, and expand on the success of the employer-sponsored retirement system

- (1) One size fits all
- (2) Misguided fiduciaries





A Solution to One-Size-Fits-All

THE NEED FOR PERSONALIZATION

PERSONALIZATION VERSUS CUSTOMIZATION

FORM: THE ROLE OF MODEL PORTFOLIOS



One-size-fits-all

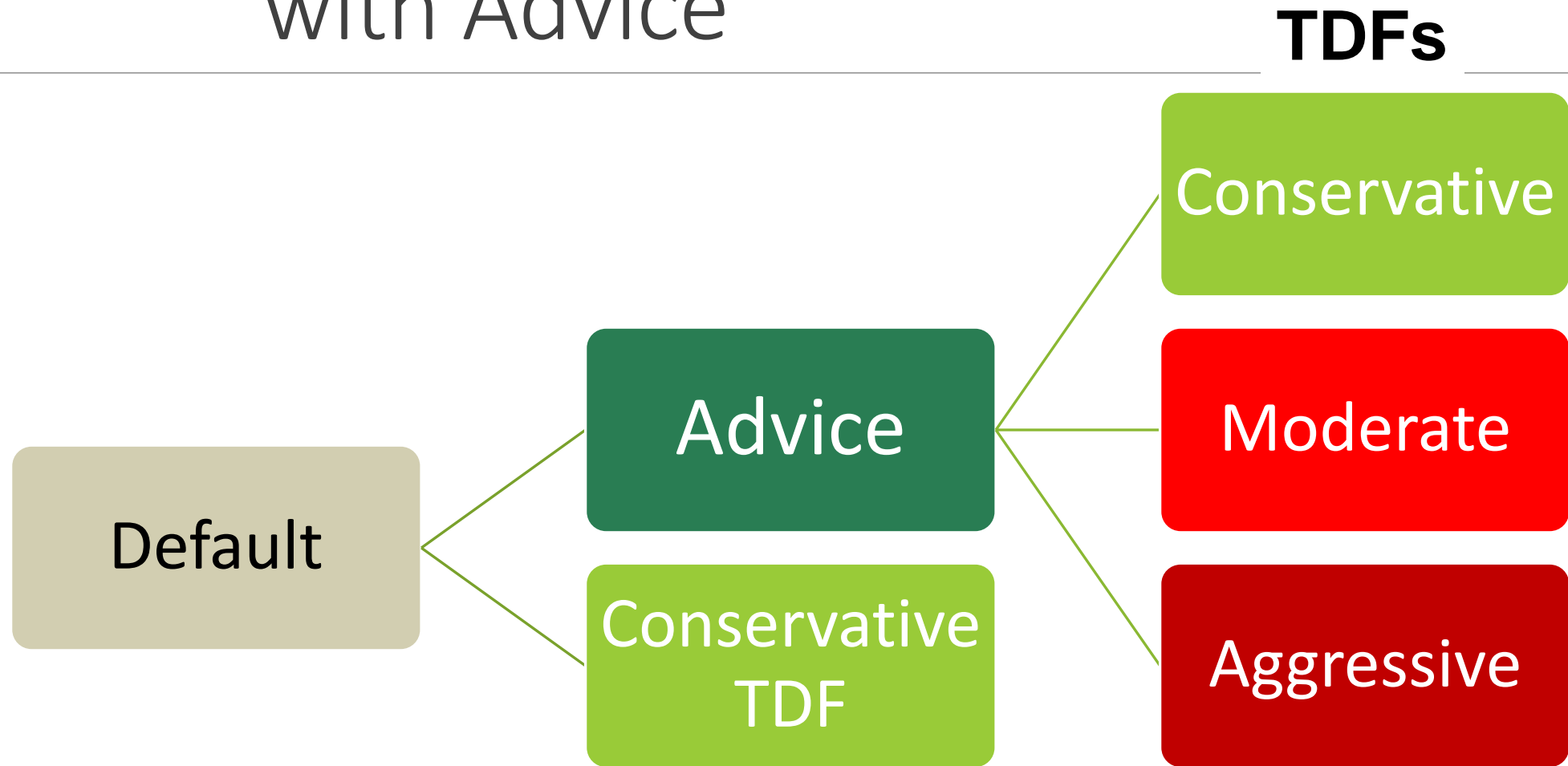
Beneficiaries have unique needs and wants.

This is the one problem that is acknowledged by everyone. Providers have tried to solve the problem with **Custom** TDFs and “**Hybrid** TDFs” that roll old people out of TDFs and into Managed Accounts.

Custom is still one-size-fits-all

Hybrids will only work with live advice rather than robo/virtual. A defaulted participant is not likely to engage in an automated decision process.

Complementing Target Date Funds with Advice



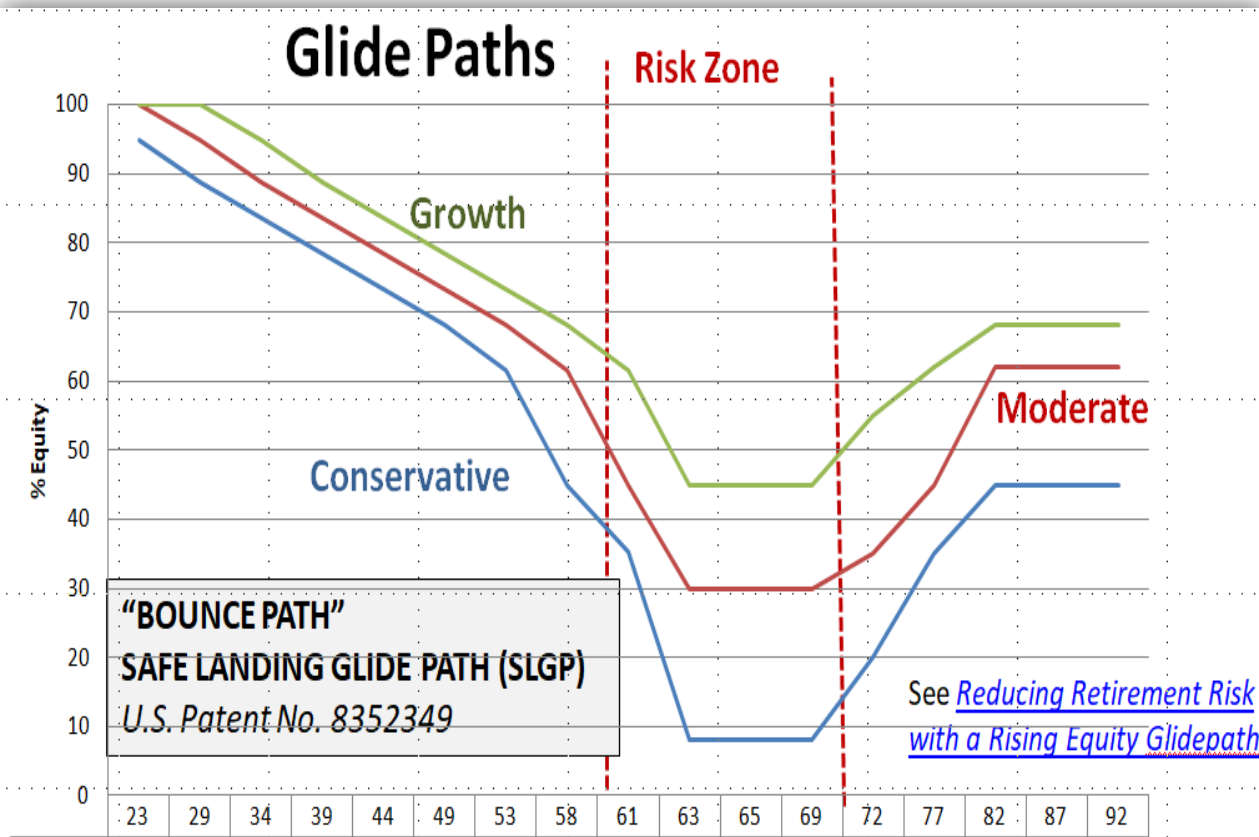
Solution

Personalized Target Date Model Accounts

Beneficiaries have choices of TDF risk-based glide paths: low, middle or high risk. The default QDIA is low risk. Non-defaulted participants can change their risk selection at will.

The recordkeeper is the key, transacting to move each participant along their selected path.

Can be very low cost. Less than 10 bps



Fall, 2018 issue

Please Read

DEFINED CONTRIBUTION **Insights** The Solution Source for Plan Sponsors

Fall 2018 • Vol. 66, No. 3

403(b) Research

2 PSCAs 2018 403(b) Plan Survey

Non-profit organizations continue to improve their 403(b) plans.

By Hattie Greenan

Plan Design

6 New DOL Guidance on ESG Investing

Plan sponsors may want to evaluate Environmental, Social, and Governance (ESG) factors when evaluating the plan's investment offerings.

By Robert E. Pike and Matthew W. Sherwood

HSAs

10 Aligning Medicare, Healthcare in Retirement, and the HSA

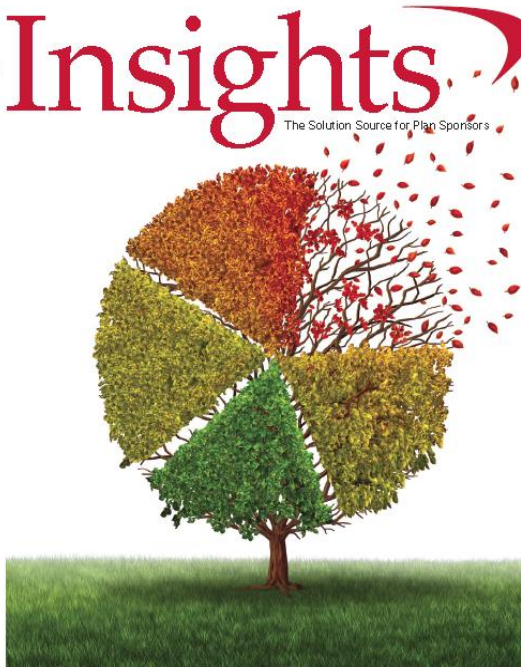
Education and access to HSAs can help employees understand how Medicare works, and the true cost of healthcare in retirement.

By Karin Rettger and Pat Jarrett

Plan Administration

12 Emergencies: A Matter of When, Not If

Considerations for employers to



Investments

1 Target Date Model Portfolios

Using a plan's core lineup to create target date models can provide lower cost and higher transparency.

By Ron Surz and Jack Towarnicky

IN EVERY ISSUE

Leadership Letter — page 1
Aging retirees face big financial decisions with perhaps less cognitive ability. Staying in the plan post-retirement may offer the best support for those individuals.

Retirement Ready! — page 5
The "gig" economy, eligibility requirements

Investments

Target Date Model Portfolios

A twist on the target-date fund approach.

By Ron Surz and Jack Towarnicky

Target Date Funds (TDFs) are the fastest growing investment in individual account retirement savings plans because they are the most popular Qualified Default Investment Alternative (QDIA).¹

But the use of TDFs as the QDIA is still in its infancy, having effectively been launched with the passage of the Pension Protection Act of 2006 and subsequent Department of Labor regulations.² So there is opportunity for innovations and improvements. Here, we offer one such innovation, target date models (TDMs).

TDFs can be viewed as a sequence of target risk models on cruise control, as shown in Exhibit 1. The typical TDF is a mutual fund or fund of funds or a collective investment trust (CIT) incorporating a collection of target risk model portfolios and a glide path that will be followed as participants age, moving investment allocations from high risk to low.

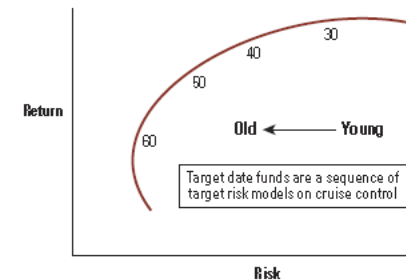
TDMs are a set of electronic investment instructions that specify both the collection of risk portfolios and the glide paths. Where the TDM is

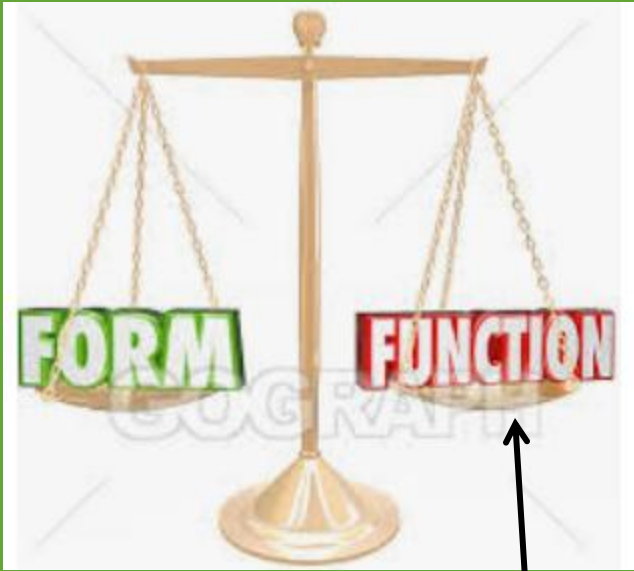
deployed as a QDIA, a default glide path is created and deployed for each TDM. The plan's investment fiduciary can also adopt additional TDMs with other glide paths — so participants can move between TDMs with different glide paths should their situation change. Here the record keeper treats each TDM exactly as if the participant had made an affirmative investment election to allocate account assets across the core investment options used in the model.

The TDM offers:

- **Transparency:** Because the TDM only uses an allocation across core investment options, the TDM is fully transparent to participants — they see the actual allocations whenever examining their account balance, and, they are notified whenever the model is rebalanced as the participant approaches the target date. Since all holdings in the TDM are in the core investments, details on

Exhibit 1: Return vs. Risk





Manage to
Objectives



These Bogus Objectives are Mere Hopes

Replace Pay

Manage Longevity Risk

Saving enough is the key to achievement, not investment performance.

The Real Objective:
Everyone wants to
be protected

Fiduciaries

(Advisors and Sponsors)
view the Big 3 as a Safe
Harbor

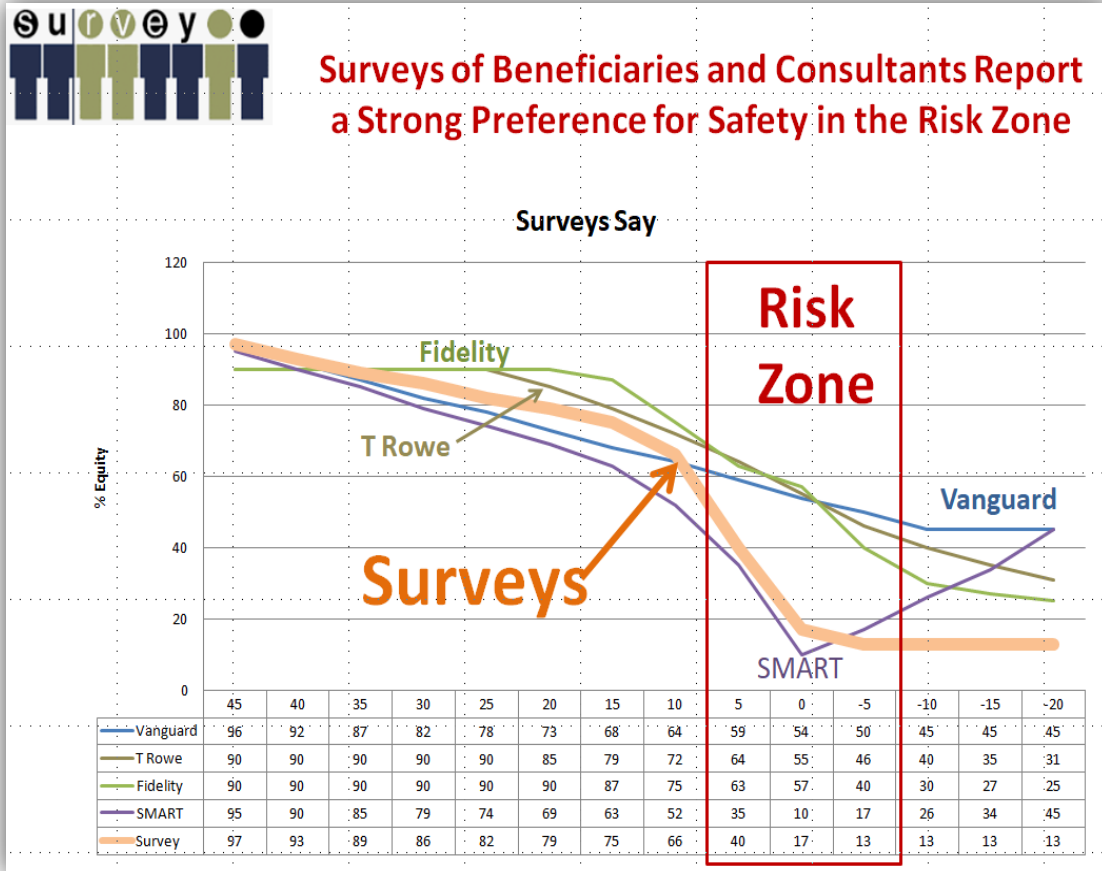
Beneficiaries

Want preservation,
especially near retirement





Surveys Report Preference for Safety



Beneficiaries & Consultants Want Asset Protection

[MassMutual Retirement Savings Risk Study](#) examines beneficiary risk preferences in 401(k) plans.

Pacific Investment Management Company (PIMCO) conducted another survey entitled the [“2018 12th Annual DC Consulting Support & Trends Survey”](#).

U-shaped **SMART TDF Index** is real & is best fit for the 20 years spanning the decade before & after retirement

Whose Objectives Should be Served? Who is the “Client”?



I want protection from lawsuits

Big 3



Sponsors & Advisors

Beneficiaries



I want protection from investment losses

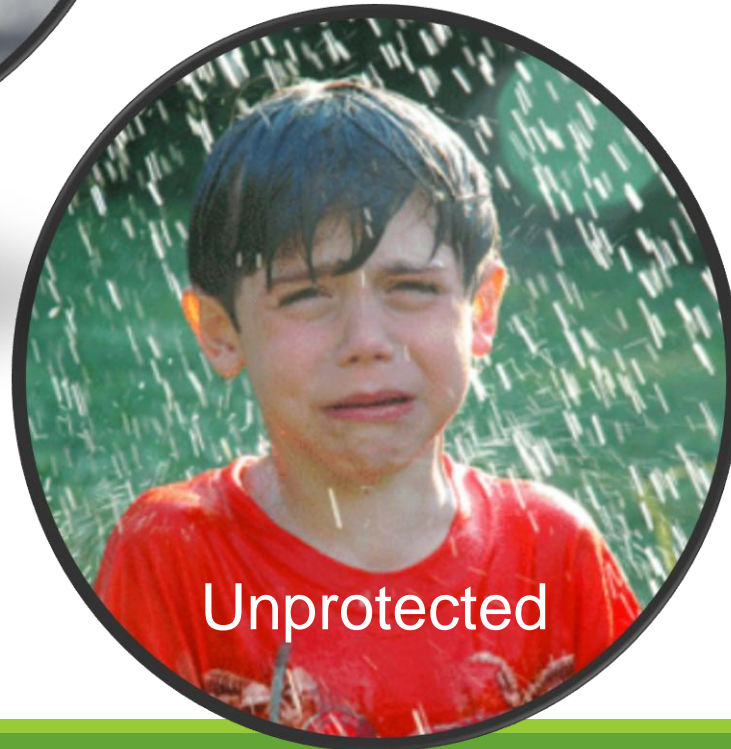
Not the Big 3



Misguided

Advisors think the Big 3 oligopoly is a safe haven

Beneficiaries are not getting what they want & need



Unprotected

Common Practice

The “Clients” are Plan Sponsors

Advisors choose TDFs. The advisor’s clients are plan sponsors. That’s who writes the checks.

The plan sponsor’s responsibility is to the beneficiaries. The duty of care requires protection from avoidable harms.

Sponsors (the Clients) want to avoid lawsuits & attorneys tell them that procedural prudence is the answer.

Sponsors want to protect themselves, even if it means unintentionally endangering their beneficiaries. Advisors also want to protect themselves. Everyone wants to be protected.



Sticks work.
Carrots don't

The Duty of Care

Fiduciaries are responsible for harm to their beneficiaries that should have been avoided



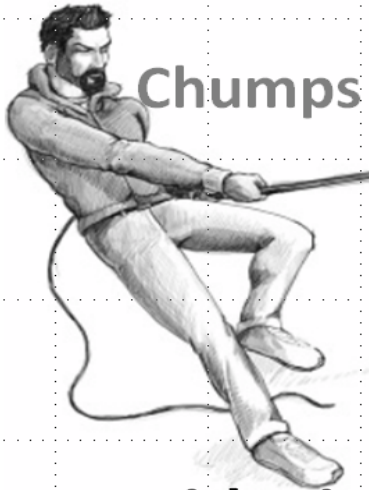
Fiduciaries Are Not Getting the Protection They Think



“Pure heart and empty head” is no excuse.

We have a winner...

**Conflicting Interests
in Target Date Funds**



Chumps

**Fiduciaries
No Lawsuits**



**Winners
Investment
Managers
\$\$ Profits**

Losers



**Beneficiaries
Safety & Growth**

**The Law is in this corner:
“ERISA protects the assets of employees”**

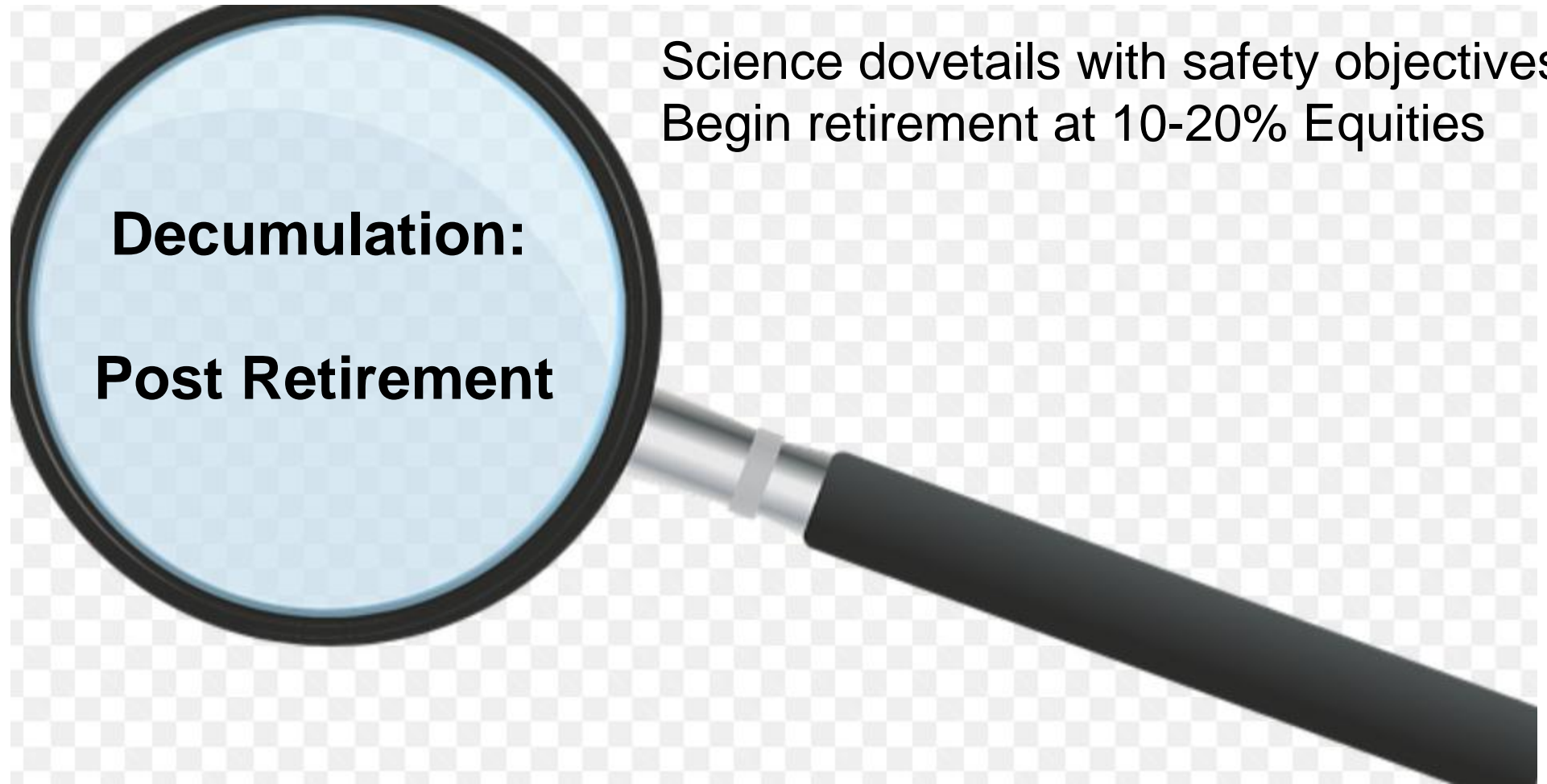
2 More Reasons to Protect at the Target Date



Meet beneficiary & advisor objective of not losing money

➤ Optimize post-retirement glidepath

➤ Current threat of market correction (Reinforces Risk Management)



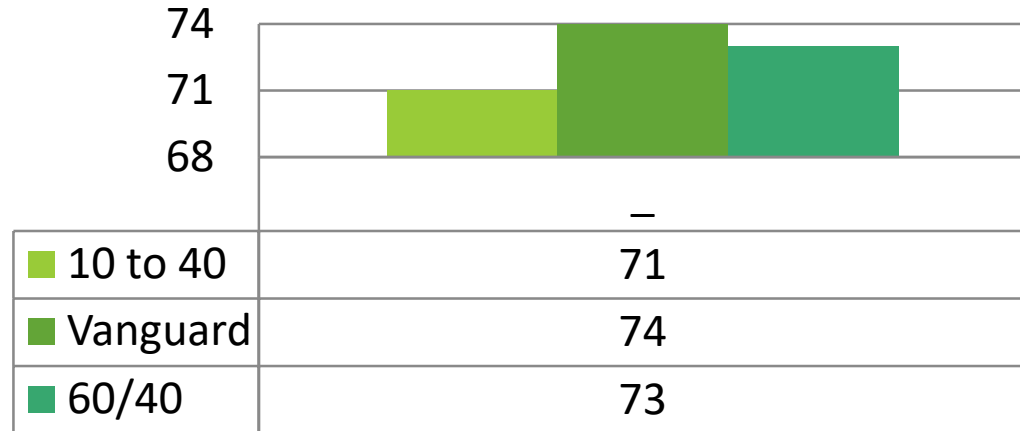
Decumulation:

Post Retirement

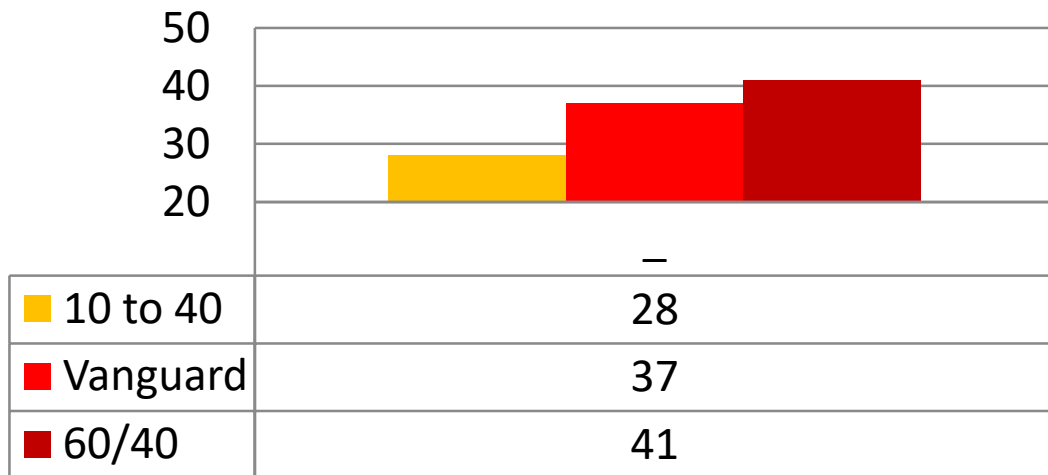
Science dovetails with safety objectives:

Begin retirement at 10-20% Equities

Probability of Success



Major Shortfall Risk(Very Broke)



Post Retirement Academic Research Supports Increasing Risk in Retirement

[Reducing Retirement Risk With a Rising Equity Glidepath.](#)

Same probability of success with better protection

[Dr Wade Pfau](#) Ph.D and CFA, is Professor of Retirement Income at the American College of Financial Services


[Michael Kitces](#) MSFS, MTAX, CFP, CLU, ChFC, RHU, REBC, CASL, is a highly regarded financial planner who holds Masters Degrees in Financial Services and Taxation, plus extensive professional designations

Also [Richard Fullmer's Framework for Portfolio Decumulation](#) Uses math to prove increasing risk.

U-shape

Beginning retirement at 10% equity means ending working life at 10%. Then increase risk to increase life of investments.

1 More Reason to Protect at the Target Date

 Meet beneficiary & advisor objective of not losing money

 Optimize post-retirement glidepath

➤ Current threat of market correction



Protect Against “Crash” Landing

RISK MANAGEMENT RATHER THAN MARKET TIMING

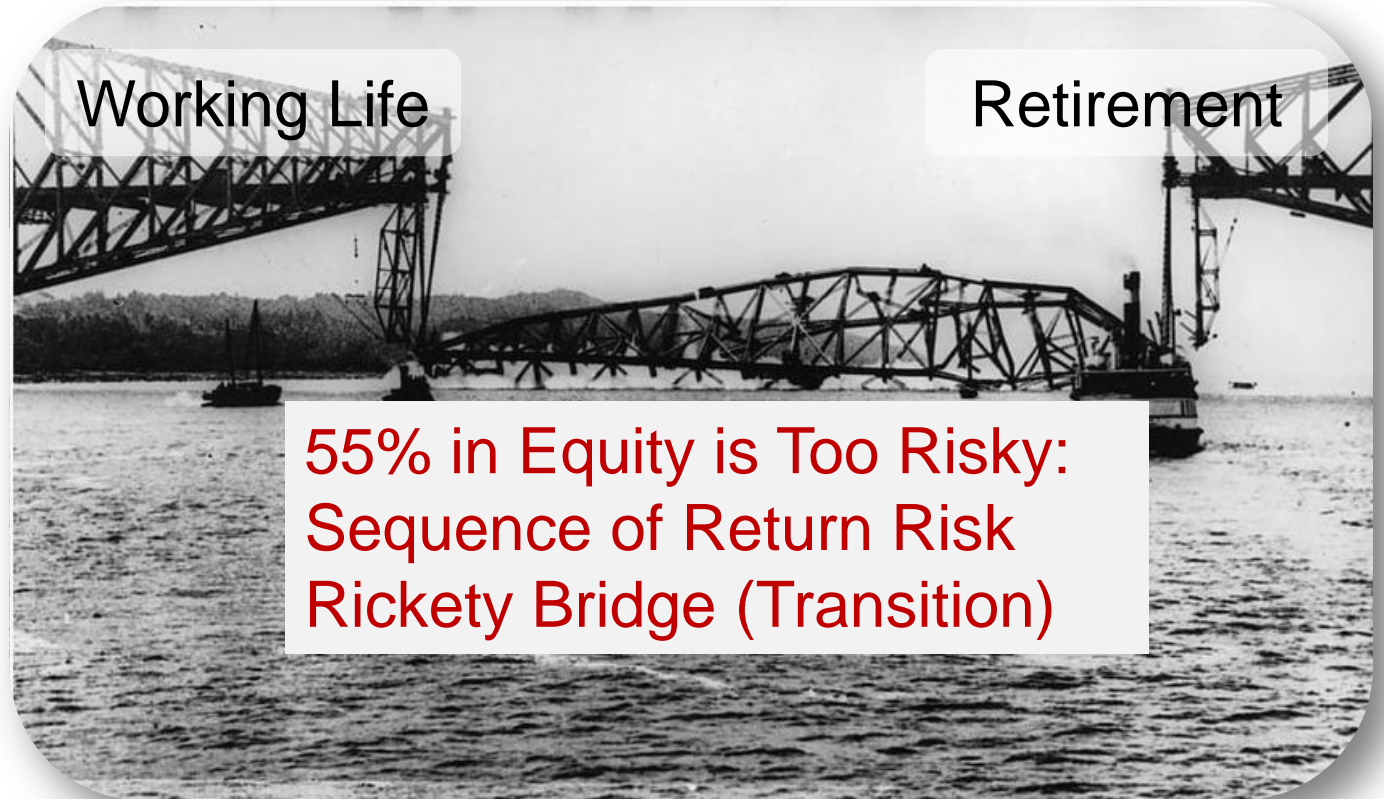
“IF SOMETHING CANNOT LAST FOREVER, IT WILL END”

75 MILLION BABY BOOMERS




TDFs are **destined to collapse** and to devastate those near retirement

- Too risky at the target date
- No financial engineering
- Built for profit rather than protection

Target-Date Fund “Crash” Landing Points



3 Reasons to Protect at the Target Date

-  Meet beneficiary & advisor objective of not losing money
-  Optimize post-retirement glidepath
-  Current threat of market correction



Searching for a Standard

Defend in the Risk Zone

Broadly Diversify

Low Cost



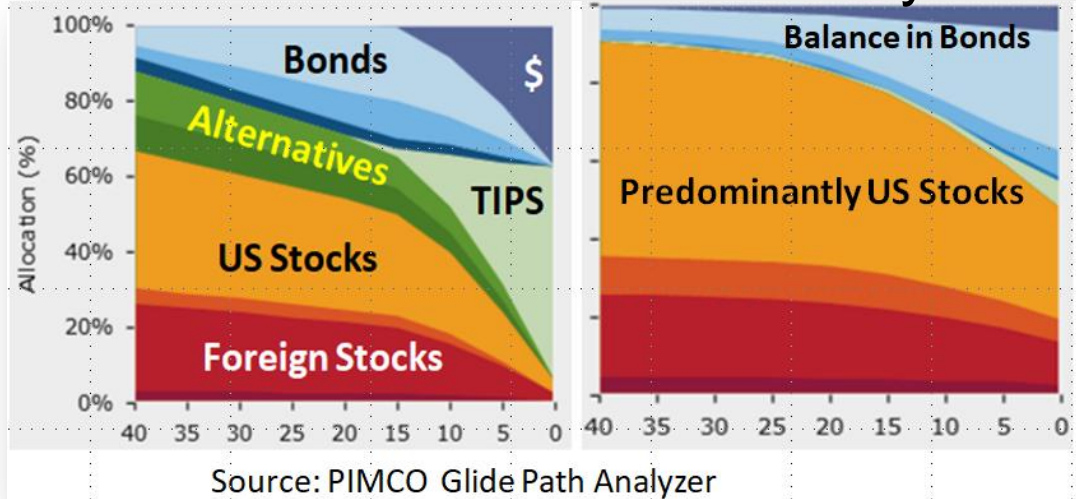
TDF Indexes

- 2007 SMART
- 2008 S&P
- 2009 Morningstar

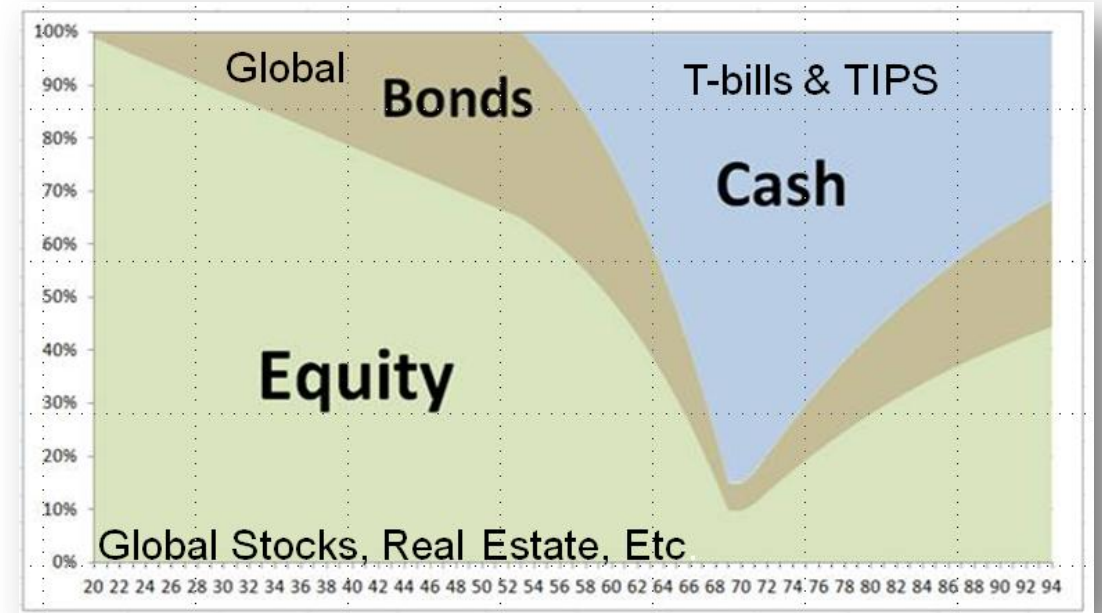
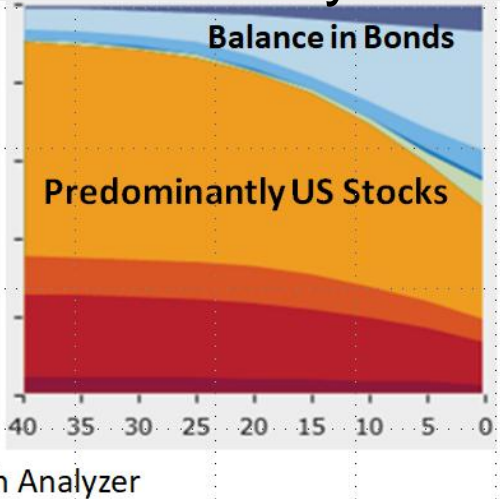


Should we be satisfied with what we have?

SMART

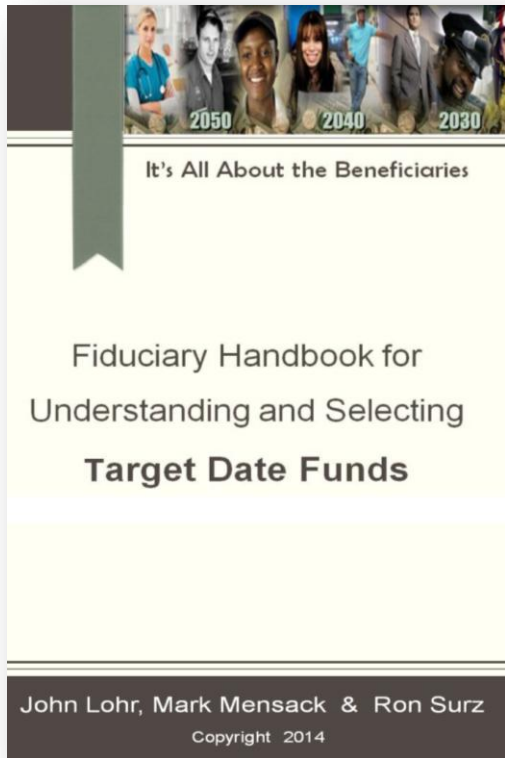


Industry

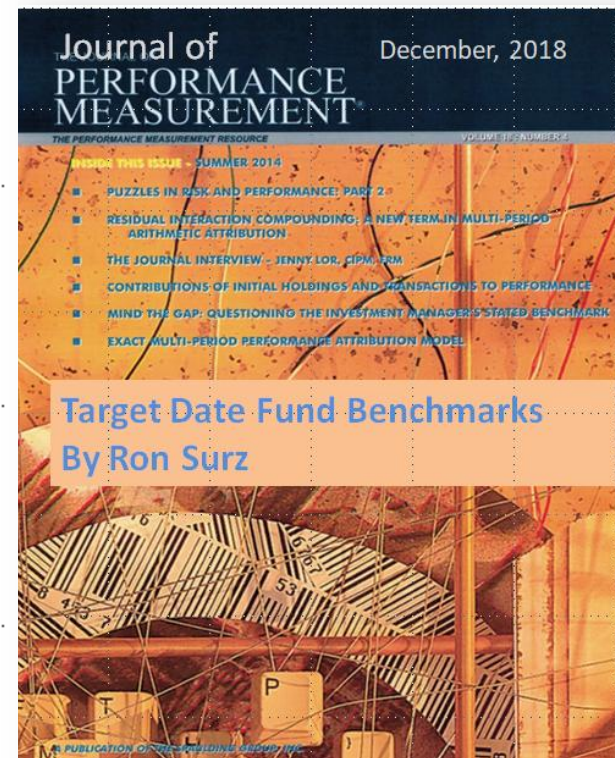


We'd do better for beneficiaries with:
Very Safe at the Target Date & Broad Diversification
Personalized to Solve One-size-fits-all

2 Books



2 Articles



Recommended Reading Available on Request

Takeaways



PSCA Mission:

Solve real problems, create positive change, and expand on the success of the employer-sponsored retirement system

Personalized Solves
One Size Fits All

FORM
— AND —
FUNCTION

U-Shape Provides
Protection at Target

Recordkeeper is key



Fiduciary practices
need to improve.