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Insights on Fintech, 401(k) plans and the 2018 Pension Research Council Symposium

An Interview with Stacy Schaus

Stacy Schaus, CFP®, is an executive vice president in the Newport Beach office and leads PIMCO's Defined Contribution Practice, working primarily with plan sponsors and consultants.

The Pension Research Council 2018 Symposium was titled, "The Disruptive Impact of FinTech on Retirement Systems." Stacy Schaus was one of the panel moderators at the 2018 Pension Research Council Symposium. This interview provides some insight from Stacy. The papers offer a view of an extremely important developing area. In this interview, Stacy shares with us her personal insights on the conference and its implication for 401(k) plans.

Can you tell us a little about your background and prior work on 401(k) plans?

My career has focused on defined contribution plans such as 401(k)s since 1991 when I was a consultant at Hewitt Associates (now Aon and, separately, Alight) in Lincolnshire, Illinois. At Hewitt, I built the defined contribution (DC) investment team and founded Hewitt Financial Services and the Personal Finance Center to deliver brokerage windows for DC plans and personal financial support (e.g., retirement rollover counseling, annuity purchase, college funding and budgeting).

In 2006, I joined PIMCO in Newport Beach, California, to launch their DC practice. I work with plan sponsors and consultants on defined contribution plan design. To capture insights from the DC consultants on current and future trends, we conduct annually the PIMCO Defined Contribution Consulting Support and Trends Survey.[1] The 2018 survey captures data, trends and opinions from 77 consulting firms, the highest number in the 12-year history of the study. These firms advise on over $4.4 trillion in U.S. DC assets, accounting for almost 60 percent of all U.S. DC assets ($7.69 trillion, according to ICI Retirement Market Statistics, March 2018).

I have also published over 100 articles on DC issues and two Wiley books, including *Designing Successful Target-Date Strategies for Defined Contribution Plans* (2010) and *Successful Defined Contribution Investment Design* (2017). Both were written to help plan sponsors as they evolve their DC plan offerings.

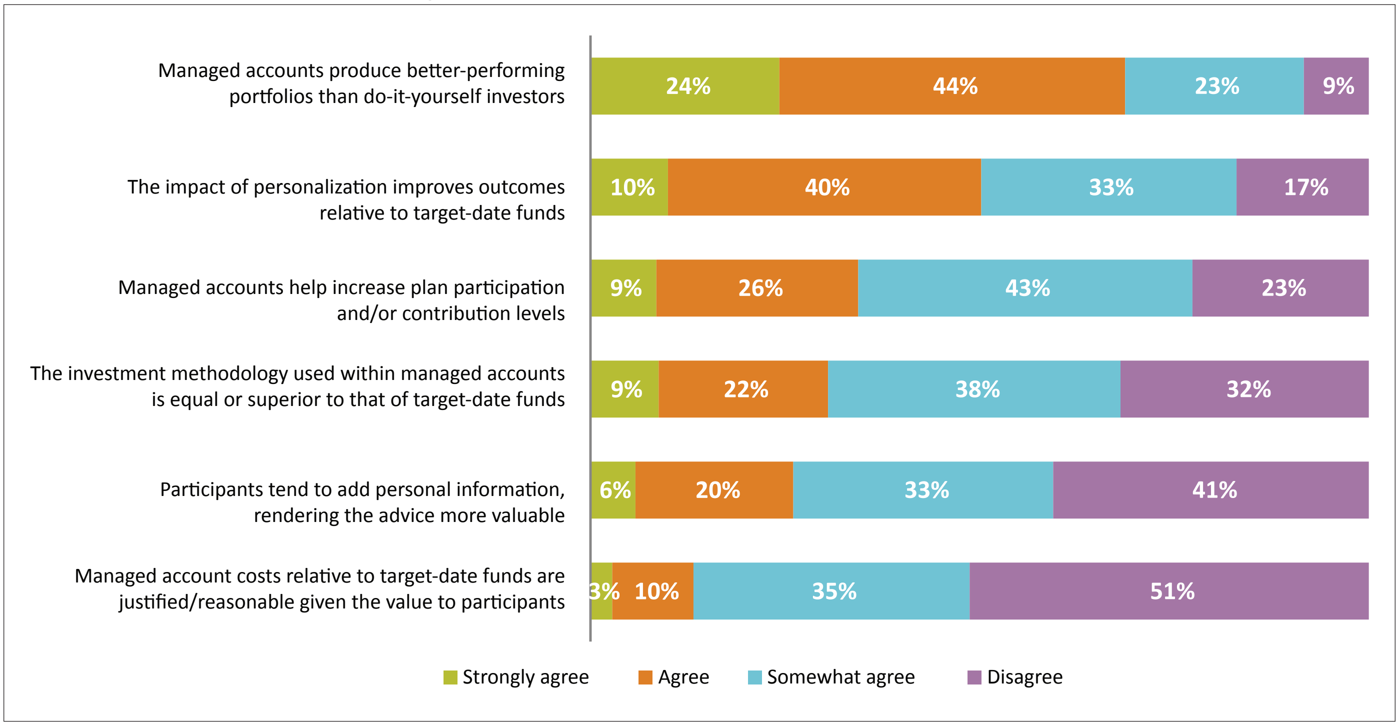
Why is this topic of FinTech important?

Innovations and continued evolution in FinTech are likely to enhance and possibly revolutionize the way people save and plan for retirement. "Robo-advice" is one example of FinTech and may include managed accounts within DC plans or full robo-advisor platforms in the retail market. These programs may include automated asset allocation and rebalancing, contribution rate suggestions, retirement income forecasting and possibly decumulation advice. As discussed during the conference, even the most advanced robo programs often offer human assistance via electronic chat or telephone.

As the moderator for Session III: "New Roles and Responsibilities for Plan Sponsors and Regulators," I shared perspectives on managed accounts from PIMCO's *DC Consulting Support and Trends Survey*. Notably, while the government has approved managed accounts as a qualified default investment alternative (QDIA), only 3 percent of the participating consultants recommend this default type, while the majority of consultants (87 percent) recommend target-date funds as a DC plan's investment default. In this year's study, we also asked consultants to share their view on managed accounts.

Figure 1 summarizes the consultants' views. At least half strongly agree or agree with the view that managed accounts produce better-performing portfolios than do-it-yourself

Figure 1
Q: What is your firm's view on managed accounts? (n=70)



Source: 2018 PIMCO Defined Contribution Consulting Support and Trends Survey

investors (68 percent) and that the impact of personalization improves outcomes relative to target-date funds (50 percent). Yet the majority disagree on the notion that managed account costs relative to target-date funds are justified/reasonable given the value to participants (51 percent) and two-fifths disagree that participants tend to add personal information, rendering the advice of managed accounts more valuable (41 percent).

As FinTech advances, perhaps the personalization of advice models may become more automated. This may facilitate more frequent inclusion of outside assets, incorporate behavioral risk preferences, and reflect spending patterns and health data (e.g., to project longevity). Costs of managed accounts or robo advice may also be driven downward as FinTech improvements continue.

What are your major takeaways from the papers and discussions?

FinTech is unlikely to replace human interaction any time soon. Discussant Kent Smetters of Wharton noted that hiring a professional certified financial planner (CFP) can be more valuable than robo advice, as the CFP can help people more holistically with issues ranging from basic budgeting to retirement financing. FinTech tools can be more efficient, but fall short of solving for lifecycle needs.

Jill Fisch, University of Pennsylvania Law School, and Marion Laboure, Harvard University, shared a paper on "The Economics of Complex Decision Making: The Emergence of the Robo Advisor." Similar to Kent Smetters' observations, they noted that robo solutions offer advantages such as anytime access, economies of scale and lack of conflict of interest. But they also have disadvantages, including the lack of the "warm body effect" (i.e., the value in talking to someone, which can make people less risk-averse), reduced effectiveness relative to an advisor in informing investors, and less flexible approaches to risk tolerance (i.e., risk preference is not stable).

What surprised you the most? What was the most concerning or eye-opening?

I found the discussion of cybersecurity and genetic data particularly eye-opening and concerning. Papers by Tim Rouse of SPARK, David N. Levine and Allison Itami of the Groom Law Group, and Ben Taylor of Callan Consulting were particularly notable. "*Benefit Plan Cybersecurity Considerations: A Recordkeeper and Plan Perspective*," addressed the issue of cybersecurity. Ben Taylor observed that "data is the new oil" and stressed the

need to vigilantly protect participants against data breaches and data attacks.

Columbia University Medical School Professor Robert Klitzman spoke on the topic of, "*Ethics, Insurance, Pricing, Genetics, and Big Data.*" He discussed the ethical issues around the use of genetic information. He notes in his paper that genetic testing company 23andMe has sold genetic data (e.g., it sold data of about one million consumers to a pharmaceutical company for $60 million in 2015). Concerns about discrimination could lead individuals to avoid genetic testing, e.g., insurance availability or pricing. Also, those who know their genetic information (e.g., the probability of getting Alzheimer's disease) may buy insurance that creates an adverse selection risk for insurance companies.

What is particularly important to people who are either leaving benefit plans with assets or retaining assets in plan?

Several speakers acknowledged the need for improvements in the retirement spending phase. Steve Polansky and Peter Chandler of FINRA discussed their paper with Gary Mottola, "*The Big Spend Down: Digital Investment Advice and Decumulation.*" They noted that the majority of robos today do not focus on decumulation, although some offer services relevant to decumulation. They pointed out that one firm offers an automatic withdrawal feature that investors can activate and that the same firm offers a more sophisticated approach to drawdowns that considers required minimum distributions. Another firm, they noted, offers a "hybrid robo service" (FinTech plus human support) that can help address more complex questions, such as determining the sequencing of withdrawals from taxable and non-taxable accounts.

Did PIMCO's *DC Support and Consulting Trends Survey* offer any insights into retirement and use of advice?

Yes, as the moderator for Session III, I shared insights on what the consultants suggest. Retirees may be more likely to retain their assets in a DC plan rather than rolling this money into an individual retirement account (IRA). DC plans may offer investments (e.g., stable value or custom strategies) that are not available in an IRA, and they may have access to institutional pricing and the benefit of a plan sponsor's oversight of the investment lineup. About 20 percent of DC assets are held by participants aged 60 or over, according to the Employee Benefit Research Institute.

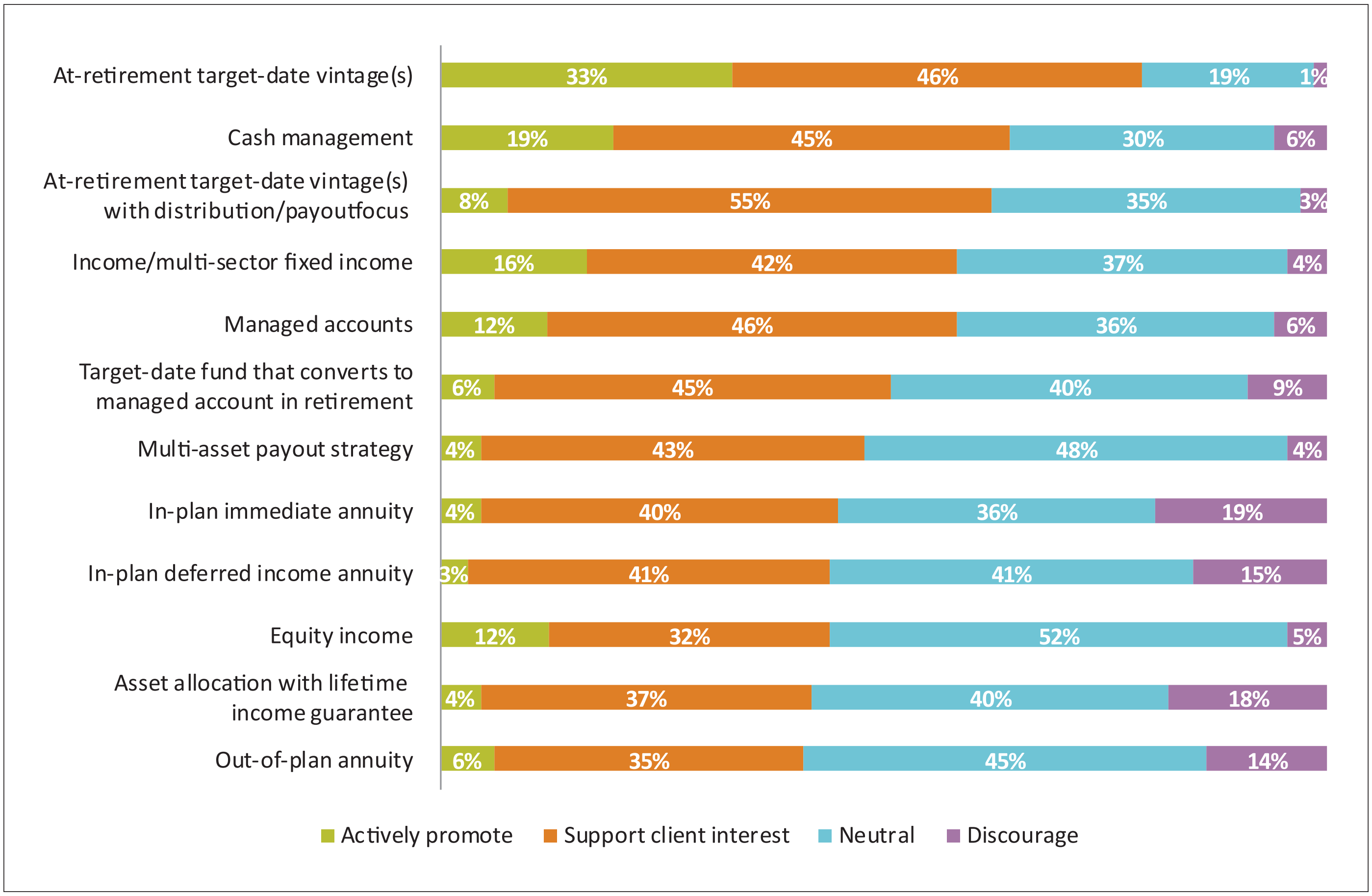
The PIMCO survey shows that the majority of consultants (64 percent) believe DC plans should offer a separate retirement income tier to their participants. This may be "in communication only (tier may use many of the same offerings as the others tiers)" or "fully set up as a separate tier." The majority of consultants support or actively promote target-date funds, cash management (such as stable value), income/multi-sector fixed income for retirees and managed accounts. It is notable that managed accounts or "robo advice" falls lower on the list of support by consultants, perhaps again reflecting the concerns with relative value of the managed account advice (see Figure 2).

How can these developments improve retirement security?

FinTech in its broadest definition can increase retirement security immensely. If one considers the enormous investments already made in the past few decades in DC recordkeeping, participant communication channels, and advice and education, one can already see dramatic improvements in retirement security. The combined adoption of auto-plan enrollment, auto-deferral escalation, and automatic dynamic portfolio management (e.g., target-date funds) is a salutary example. Collectively, these advancements—all facilitated by technology—are leading millions of participants to far greater wealth accumulation potential than would have otherwise occurred.

Yet, the final roundtable session, "The Future of Retirement Startups: Challenges and Opportunities," revealed FinTech

Figure 2
Q: What is your firm's position on the use of the following investment and insurance retirement income strategies?* (n=67)



*Responses ordered by the sum of "Actively promote" and "Support client interest"

Source: 2018 PIMCO Defined Contribution Consulting Support and Trends Survey

can help address an enormous and growing retiree need: generating sustainable income in retirement. Debra Whitman of AARP referred to this as the "Big Spend Down," stating that it is a huge, complex and complicated issue. Rhian Horgan of internet startup Kindur.com explained their value proposition will be to help those considering retirement to know if they are ready, and assist in the process to help clients enjoy this phase of their lives. Elizabeth Kelly of United Income Inc. shared that the myriad of questions one faces when considering retirement creates fear, with the result being many people reduce their spending. A noteworthy observation made by all on the panel is that retirement presents decisions never previously considered. Examples included the election of Social Security and Medicare benefits. Clearly, FinTech will provide new decision-making and support services, leading to better outcomes for many. ■

Note: Joseph Healy, senior vice president and DC Specialist at PIMCO, contributed to this article.

ENDNOTE

1 *https://www.pimco.com/en-us/dc-survey*