SOCIETY OF ACTUARIES

Investment and Retirement Advice

A Guide for Employers

About this guide

The Society of Actuaries' Committee on Post-Retirement Needs and Risks (CPRNR) commissioned Linda Koco to write this guide that employers can use when considering advice options for a company retirement plan. The guide includes information about the nature and timing of decisions, ongoing decisions after retirement, and advice considerations. The guide is intended to be unbiased toward any particular approach or organization's product.

The author, Linda Koco, is a sole practitioner with extensive insurance writing and editing expertise in the area of retirement income planning and issues.

The CPRNR would like to thank the Project Oversight Group for input on the content and review and oversight of the project: Andrea Sellars, Anna Rappaport, Betty Meredith, Carol Bogosian, Cindy Hounsell, Elvin Turner, Greg Gocek, Greg Ward, Joe Tomlinson, John Migliaccio, Kelli Hueler, Linda Stone, Lynn Franzoi, Paula Hogan, Rick Miller, Andy Peterson, Steve Siegel, and Barbara Scott.

Investment and Retirement Advice

A GUIDE FOR EMPLOYERS

Employees at a regional manufacturer often went to the human resources department seeking advice and asking questions about their 401(k) plan: How much to contribute? Which investment options to choose? How to use the savings for retirement? This happened so often that HR suggested the company consider including an advice service in the company plan. The officers agreed to look into it. Once they did, they found they had a lot to learn—and a lot of their own questions: What type of advice will work for the employees? How to manage cost and effectiveness? Will we be liable as a fiduciary for the advice? Will this help us recruit and retain workers? Will it contribute to productivity by making workers feel more secure? Where to start?

Plan sponsors have a lot of concerns like that about advice services in company-sponsored retirement plans. This guide provides some answers and suggested areas to think about.

Some of the material is drawn from "Models of Financial Advice for Retirement Plans: Considerations for Plan Sponsors," a 2014 study commissioned by the Society of Actuaries (SOA). The paper looks at not only the rising demand for advice but also current trends in this field. It is based on extensive research by authors Michael S. Finke, Ph.D., CFP, at Texas Tech University, and Benjamin F. Cummings, Ph.D., CFP, at Saint Joseph's University, both professors with substantial expertise in financial services.

QUICK START

- This guide uses an abbreviated format to make it easy for plan sponsors to learn more about specific advice topics. For a deeper dive, it cross-references to various sections of the paper by saying: *[See Finke-Cummings, page x.]*
- We present areas to think about when examining advice options for a company retirement plan. The guide is not, however, intended to provide legal guidance or recommendations.
- The guide avoids jargon whenever possible but defines specialized terms when first used.
- Because plans differ widely in size, scope and structure, it is helpful to have the company's plan specialist, provider, attorney or other knowledgeable professional provide input as well.
- To learn more about the Society of Actuaries, visit us at *www.soa.org.*

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Introduction

Defined contribution (DC) plans became widespread in the late 1970s and are now the dominant form of retirement plan in the private sector of the United States. The most well-known version is the 401(k) plan. Others include 403(b), 457 and the Thrift Savings Plan, and they operate under different rules and taxation principles.

Nearly all DC plans enable participants (employees who join the plan) to contribute a percentage of regular pay to the plan. The funds grow tax-deferred in the plan until withdrawn. The participants allocate their contributions to one or more investment options that the plan makes available. These options are most often mutual funds but some plans also include stocks, cash equivalents, annuities and many other choices.

In most cases, the plan sponsor (usually the employer) has preselected the investment choices following a rigorous due-diligence process. Even so, choosing from a narrowed-down list remains a daunting task for many plan participants, who may not understand the different investment options, how much to invest, or what percentage to allocate to each option. Some participants may later wonder if they should take a loan or withdrawal from the plan, or how to use plan savings to create income in retirement. Some ask bluntly, "What should I do?"

Many employers are keenly aware of these issues. As a result, employer interest in adding a financial advice component to their companies' retirement plans is rising.

The good news is that many plan providers—the investment companies, banks and insurance companies that provide retirement plans and services—now offer a number of advice solutions. So do outside plan advisers and consultants. But deciding which solution to choose brings up key fiduciary and due-diligence questions for employers.

1 What is advice anyway?

Advice refers to a recommendation about what to do or not do regarding a decision at hand. In the retirement plan community, plan service providers often stress that this is an informed opinion, and that it is "personalized" (unique) to the participant requesting it. It is what that advice provider thinks the person "should" do regarding retirement savings in the plan based on available information. The participant can choose to follow the advice or not.

Some DC plan sponsors want to know if providing advice to plan participants is mandatory. The answer is no, employers are not required to provide advice services with their DC plans. But many employers are doing so anyway. This is because advice helps employees make plan decisions even as it creates potential recruitment and retention advantages for the employer (among other benefits).

Government regulations do allow plans to offer advice options, subject to standards. For instance:

- **THE EMPLOYEE RETIREMENT INCOME SECURITY ACT (ERISA) OF 1974** says that, if investment advice is offered to participants, the advice provider must serve as a fiduciary (that is, do what is in the best interest of the participants).
- **INTERPRETIVE BULLETIN 96-1**, issued by the Department of Labor (DOL) in 1996, allows plan sponsors to provide participants with investment education that is not "advice," subject to certain requirements.
- **A FINAL RULE ON INVESTMENT ADVICE FOR PARTICIPANTS AND BENEFICIARIES (FR-2011-10-25)**, issued by DOL in 2011, allows plans to offer investment advice via use of a certified unbiased computer modeling program or an adviser compensated on a level fee basis (i.e., no variance in fee by investment selected).

Policymakers and retirement experts are increasingly urging plan providers, such as insurance and mutual fund companies, to consider offering advice options. The thinking is that this will help increase plan participant access to an informed resource for personalized recommendations.

A few words about regulation. Retirement plans are highly regulated by federal laws and supervisory bodies. Advice features are no exception. In addition, those delivering advice are subject to both federal and state regulation, depending on their licensure. The regulators do not always act in a unified fashion, but in the evolving area of advice, they are definitely applying close scrutiny to establishing regulatory guidelines where needed. The box shows some key federal regulations now impacting advice.

Key federal laws impacting advice

The Securities Act of 1933 ushered in federal regulation of securities.

The Securities Exchange Act of 1934 created the Securities and Exchange Commission (SEC) to regulate securities markets and protect investors. Together with the '33 Act, the laws govern the buying and selling of securities.

The Investment Advisers Act of 1940 governs the behavior of registered investment advisers (RIAs) who are held to the fiduciary standard.

The 1938 Maloney Act authorized a self-regulatory organization—today called the Financial Industry Regulatory Authority (FINRA)—to oversee brokers-dealers, which buy and sell securities and are held to the suitability standard.

The Employee Retirement Income Security Act of 1974 (ERISA) set minimum standards for qualified retirement plans in private industry and said that plan sponsors and plan asset managers must adhere to the fiduciary standard.

The Pension Protection Act of 2006 included provisions allowing employers to auto-enroll employees into the company retirement plan. It also established a safe harbor from fiduciary liability for plan sponsors in specific areas, and slightly increased participant access to advice.

The Dodd-Frank Act of 2010 called for review of regulations governing financial advice in the retirement plans as well as in the individual securities markets. Work on this is continuing.

Note: Advisers may also be regulated by state insurance and securities regulatory agencies, depending on how the advisers are licensed.

2 Why is advice important?

Advice is important because plan participants need it, as many plan sponsors know from the stream of questions they keep getting from plan participants.

The decline in availability of defined-benefit (DB) plans (traditional pensions), and their replacement by DC plans, has contributed to this need. DC plans require participants to make decisions regarding their retirement income that professional managers make on employees' behalf in DB plans. In addition, many baby boomers are reaching the age where they realize that their plan assets will provide a portion of their retirement income—most likely for the rest of their lives.

This evolution in participant thinking has added urgency to the need for advice. Add to this several related trends such as: Americans are living longer than previous generations; the number of workers with DC accounts is higher than ever before; many Americans demonstrate low financial literacy rates; and projecting retirement income is proving to be a complex undertaking for many people. *[See Finke-Cummings, pages 24–27.]*

In this world, DC plans are taking on a greater role than ever in retirement planning. In fact, 78 percent of workers who were in a retirement plan at work in 2012 said they considered their DC plan to be their primary retirement plan, according to the Employee Benefit Research Institute (Copeland 2013). That is almost three times the level found in 1988. Unfortunately, many workers have little to no experience in investing or creating retirement security. This makes access to advice increasingly important.

OFFERING ADVICE IS IMPORTANT FOR PLAN SPONSORS TOO.

Consider:

- It may help reduce the stress and confusion that workers have about DC plan decisions, enabling employees to focus more on their duties.
- It may help strengthen employee satisfaction with the company's retirement benefits and confidence about retirement security, thus engendering loyalty and commitment to the employer.
- Workplace turnover may decline and overall productivity may increase as a result, thus adding to the value the employer derives from dollars spent for retirement plan benefits.
- It may fulfill the employer's deeply held conviction that the company should provide employees with advice resources which can help them with retirement planning.

3 How does investment advice differ from retirement advice?

Advice is a huge topic, with themes that reach beyond the scope of this guide. But plan sponsors will need to stay abreast of two main types of advice that are likely to touch the vast majority of plan participants. These are investment advice and retirement advice. *[See Finke-Cummings, page 18.]*

- **INVESTMENT ADVICE** provides personalized guidance on investment options and strategies. Such advice can be provided to plan sponsors as well as to individual participants, but our focus here is on participant-level advice. This type leads to recommendations based on a participant's risk tolerance and capacity, goals and needs, and includes advice about asset allocation, asset classes and related matters. It focuses on building up assets that will eventually fund the participant's retirement.

- **RETIREMENT ADVICE** is also personalized to the participant. It includes recommendations on not only accumulating retirement assets but also, as retirement draws near, on how to spend and distribute those assets once retired. Currently, many boomer participants are reaching the age where they start exploring how much money they will need each month to live comfortably in retirement. They also need information about withdrawal rates, likely lifespan, role of other household assets, tax-efficiency and related matters. The focuses of advice, and even the types of recommended investments, shift accordingly. Some advice services may even help the near-retirees with questions about when, where and how to retire, as well as certain health and long-term-care matters.

Some people speak of retirement advice as a component of investment advice (or the other way around). This reflects growing recognition that the two are linked. *[See Finke-Cummings, page 19–24.]*

The DOL regulations on advice currently focus on investment advice, not retirement advice. But this is a developing area, and some plan options already include retirement advice components or capabilities, at least up to the day of retirement.

This area is important to follow, since need for retirement advice, including advice for workers with modest retirement savings, is increasing. For participants who do not have advisers, the DC plan may be the one place where they could receive personalized assistance, if offered, on when to retire, retirement spending, etc.—even if they don't need much advice on investments.

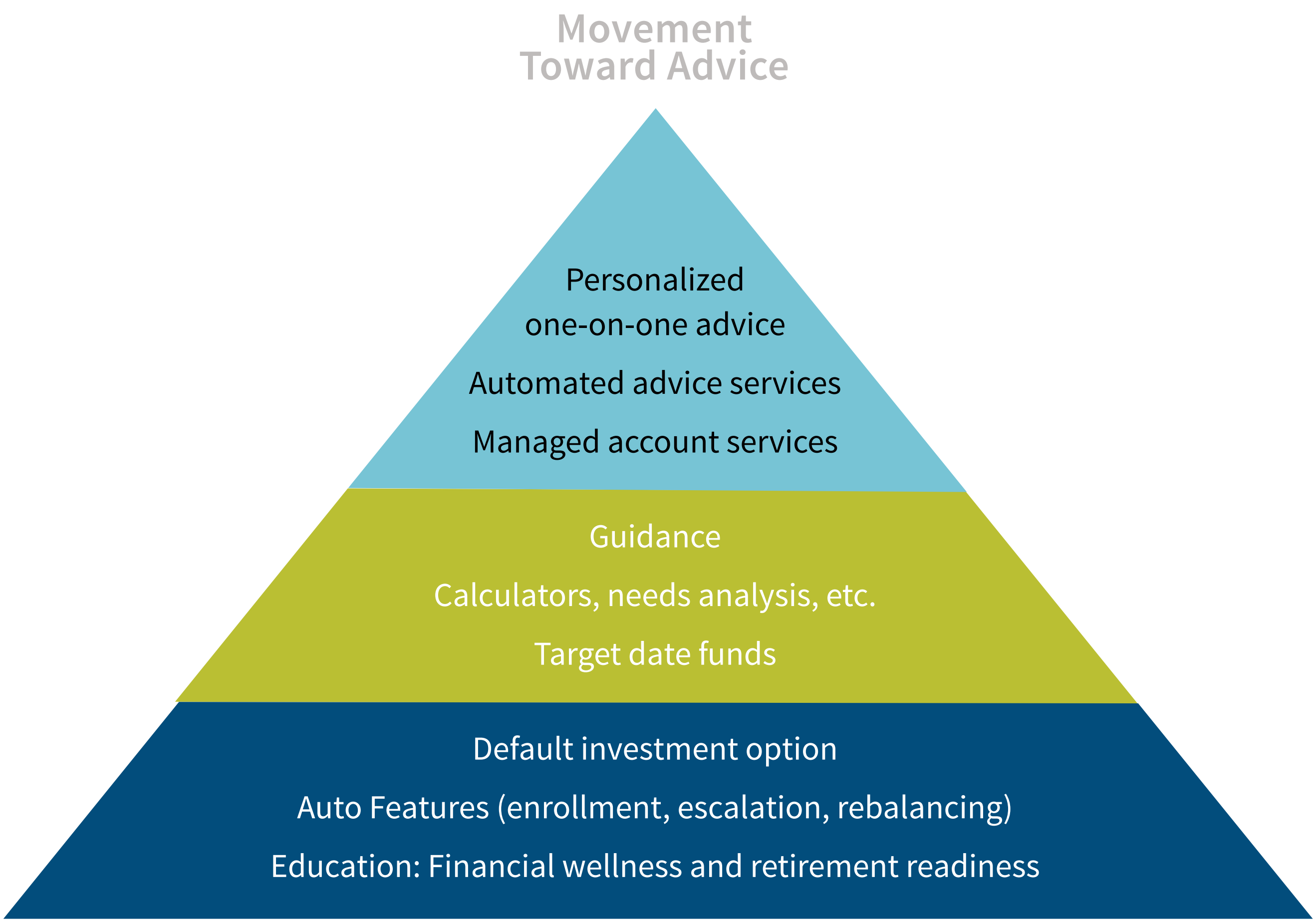
SOME QUESTIONS TO ASK

- How many of our employees need investment advice, retirement advice or both?
- How many of our employees would use the help if offered?
- What communications can we use to encourage employees to use the advice?
- What advice options fit with our philosophy on financial wellness?
- What does it cost to add advice options to our plan?
- What is our liability for offering guidance or advice?

P.S. For people with little or no retirement assets, retirement advice is key. They have a difficult path ahead and need to make careful choices.

4 What types of investment advice are there?

Today's DC retirement plans offer investment advice options of various types. The pyramid below provides an overview of common categories currently available. We've arranged them in three color-coded groups, starting from the foundation of broad-based information and moving up to personalized one-on-one advice. Some include elements of retirement advice.

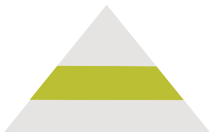


The bottom three categories provide a foundation for informed decision-making, but they are not personalized advice as discussed in this guide.

- **EDUCATION** refers to services that inform participants about plan features, investment options and, in many cases, related areas. The other areas may include financial and retirement literacy (understanding key terms and concepts), financial and retirement planning (creating a formal program to achieve desired goals), and financial and retirement wellness (programs that nudge plan participants to adopt a holistic approach to their financial behaviors and retirement savings). Plan providers often supply the education, sometimes partnering with third-party retirement education specialty firms.

- **AUTOMATIC FEATURES** include auto enrollment, auto escalation and auto rebalancing. Their purpose is to help DC participants grow savings without becoming deeply involved. The features automatically enroll workers into plans, automatically increase the workers' contribution percentages (usually annually), and automatically rebalance investments between accounts on a periodic basis. Plan sponsors choose which features to offer, and participants can opt out. The DOL, in *Automatic Enrollment 401(k) Plans for Small Businesses*, pointed out that auto enrollment could help cut worker nonparticipation in plans by at least half. That could provide employers with "an important long-term benefit that will help you attract and retain qualified employees," according to the DOL. However, plan sponsors need to be aware that, because many DC plans are structured to have matching contributions from the employer, auto enrollment and auto escalation can be expensive features to add to a plan.

- **DEFAULT INVESTMENT** is a feature that directs employee contributions into a predetermined option, technically called a qualified default investment alternative (QDIA) when a participant does not make his or her own investment selection. The purpose is to help participants get going on establishing a savings program. Under government rules, the QDIA can be a lifecycle or target-date fund (most common type), a balanced fund or a managed account. Participants can opt out. Some people view the default-to-QDIA as another type of automatic feature, but it makes no personalized recommendations. Worth noting: 2011 DOL regulations on default investment alternatives (*29 CFR Part 2550*) provide fiduciary relief to plan sponsors that offer QDIAs. DOL (2008) has even estimated that, through auto-enrollment plans and encouraging investing for long-term retirement savings, these default regulations will result in *$70 billion to $134 billion in additional retirement savings* by 2034.



The next three categories have elements of personalized advice, to the point that some plan providers do consider one or more of them to be advice options, or auto-advice options.

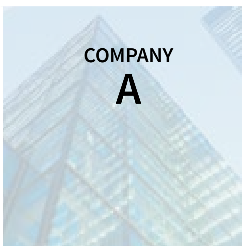
- **TARGET DATE FUNDS** are professionally managed investment options that gradually adjust the asset allocation to more conservative options as the participant approaches the selected retirement year. The targeted risk level and structure of comparable funds can vary widely. Some people consider these funds to be a type of advice because the participant chooses the target retirement date based on his or her own intended retirement date. However, these funds provide no recommendations to the participant, so they do not provide personalized advice as described in this guide. Target-date funds may be thought of as pre-retirement-oriented investment options since they normally do not provide for any change in the post-retirement period.
- **CALCULATORS** exist in an amazing array and with various underlying assumptions. Some give projections on how long a person might live. Others compute the impact of compound interest, loans taken, savings percentages, extended retirement dates, household assets beyond the plan and more. These tools do provide somewhat personalized information, based on information the participant supplies—such as how much a person needs to save—but they usually do not provide recommended courses of action. Since calculators vary in the questions they answer, the input they require and the assumptions they use, participants need to be sure the tools and assumptions used are suitable for the situation.
- **GUIDANCE** is a service that helps identify areas to think about given a participant's unique situation, but without recommending specific steps such as which funds to select or how to allocate them. We will say more about guidance later on.

The last three categories provide personalized advice in the full sense of the term. Some plan sponsors may decide to add such a service in addition to offering education, guidance or other services.

- **MANAGED ACCOUNT SERVICES** make investment and portfolio decisions on behalf of plan participants who elect the option. This is not an investment option in the sense that a target-date fund is an investment option. It is essentially a "do-it-for me" advice service. The managed account firms professionally manage the investments based on each participant's unique information, and some of them permit entry of household level data beyond the benefit plan. The fees (typically paid by participants), investment options, allocation strategies and other factors vary considerably, according to a 2014 report of the Government Accountability Office (GAO).
- **AUTOMATED ADVICE SERVICES**, also called robo-advisers, provide an online personalized advice service. The participants enter requested data about themselves, plan assets, perhaps other assets, retirement goals and so on. The service then computes and delivers personalized recommendations, having to do with investments and even, sometimes, retirement planning. This advice can be updated regularly or as requested. Automated services vary substantially and they keep evolving and innovating, too, so plan sponsors need to compare and contrast carefully—and regularly.
- **ONE-ON-ONE ADVICE** is a service in which a credentialed financial adviser works with a plan participant one-on-one to provide personalized advice. Depending on the service, the exchanges may occur face-to-face, over the telephone, in call center contacts and/or in online venues. Many advisers like to include both spouses, since although both may accumulate separately during the working years, they tend to spend as a unit in retirement. One-on-one advice can range from focusing on specific events, such as a home purchase, to ongoing recommendations regarding in-plan investing, outside investments, retirement planning and even advice during the retirement years. Those delivering the advice can be sales people, fiduciaries or both—a point we will return to later. Depending on the program structure, the participant, sponsor or both may pay for the service.

5 Why does plan design matter when choosing investment advice services?

When evaluating which option to offer, plan sponsors will want to remember that many factors—such as DC plan structure, company mission and culture—can impact this decision. Consider:



PLAN STRUCTURE: Company A's plan may be designed in such a way that most employees invest in the plan's default (QDIA) investment option. If the participants stay with this option, Company A might see little need to offer a comprehensive advice program but might want an education-and-guidance program.

MISSION: Company B sees employee's retirement security as central to accomplishment of its mission. So it offers a robust education program and a well-balanced menu of investment options. Although many plan participants understand the basics, Company B has found that many employees are uncertain about establishing a long-term retirement plan. The plan sponsor may decide that a full-featured personalized advice service would be a highly valued and often used plan feature.

CULTURE: At Company C, the plan sponsor may have noticed that most participants are making comparatively small contributions, despite having access to an education program as well as auto escalation (from which many have opted out). This company may consider adding an advice program that not only helps participants see the impact of their contribution choices on their retirement security but which also offers to recommend a tailored plan of action for each participant.

6 How do education, guidance and advice differ?

Education, guidance and advice services are often referred to interchangeably. In general, however, the services have important distinctions.

- **EDUCATION SERVICES**, as noted earlier, help participants learn about plan-related matters such as investment options, contributions and allocations. Many programs also cover more general topics such as saving, establishing retirement goals and objectives, understanding investment risk and return, getting ready to retire, what families typically do and maintaining financial wellness (behavior that supports financial health). It does not, however, recommend that participants take specific steps. Important: Federal laws and regulations—such as DOL Interpretive Bulletin 96-1, the Pension Protection Act of 2006 amendments to ERISA, the Dodd-Frank Act of 2010, and subsequent Dodd-Frank studies and rules—do not consider education to be investment advice. *[See Finke-Cummings, pages 19-20.]*

- **GUIDANCE SERVICES** have elements of personal counsel. For instance, given a participant's unique situation, some guidance programs might nudge a participant to consider re-evaluating exposure to equities or contribution levels. Others may offer to evaluate one's personal situation, suggest options and/or respond to personal questions. Think of it as decision support that stops short of providing recommendations about what a participant should do.

- **ADVICE SERVICES** make specific recommendations for a participant based on an evaluation of the person's circumstances, needs, goals and related matters. A recommendation may, for example, lay out steps the participant should take to reduce equity exposure. Some advice services will complete the action if the participant agrees, while others may leave completion to the participant. Some advice services acknowledge that they are a fiduciary giving investment advice for a fee under ERISA.

Here is a chart that highlights some other attributes of the three areas.

Education, Guidance and Advice				
Type	Purpose	How delivered	Provider	Compensation
EDUCATION	Conveys information	Website, print, seminars, benefit statements, custom e-mails, etc.	Plan sponsor, third party administrator, or separate provider	By fee, explicit or bundled
GUIDANCE	Provides decision support	Participants ask questions; service gives unbiased answers and analysis but no recommendations	Plan sponsor, third party administrator, or separate provider	Can be by task, participant, time spent or bundled
ADVICE	Recommends specific actions for a participant to take	Wide variety, ranging from automated services through one-on-one advice arrangements	Plan sponsor, third party administrator, plan provider or advisory firm inside or outside the plan	Can be fee paid by plan or participants, whether ongoing or event-based, plus other arrangements

Source: Anna Rappaport, Anna Rappaport Consulting, Chicago

SOME QUESTIONS TO ASK

- What type of help do our participants regularly request?
- Would education or guidance be sufficient or is personalized advice the dominant need?
- How do we know whether the education provided is independent and unbiased?
- When are online income calculators and similar tools considered education, guidance or advice?
- Under what circumstances is advice most important?
- How do we monitor the providers of education, guidance and/or advice?
- How do we make sure that we agree with the information and advice provided?

7 Who or what provides personalized advice?

Traditional and emerging advice services are helping to create a new image of advice and also a lot of choice—and decision-making—for plan sponsors. *[See Finke-Cummings, pages 29-30.]* The list below illustrates a spectrum of financial advice models available today.

Spectrum of financial advice models

1	Financial adviser develops and regularly updates a participant's financial plan via systematic process
2	Financial adviser provides one-on-one advice on ad hoc "event" basis
3	Plan participant inputs details into an automated system with support from an individual at the electronic advice provider
4	Plan participant inputs details into an automated system and obtains ad hoc support from a financial call center
5	Plan participant inputs details into automated software that provides specific recommendations but little or no individual support

8 What are automated advice systems?

DC retirement plans have been allowed to use unbiased computer models for advice since DOL issued new rules in 2011.

Those rules spurred development of various electronic services. As noted earlier, they are often called robo-advisers. That's in recognition of their electronic backbone, not any type of robotic structure. They may offer not only investment advice but also retirement advice. Some include financial wellness services as well.

These automated services are emerging rapidly so plan sponsors will want to do periodic online searches about them as part of their advice-selection due diligence. Some common features in the current market include:

- Service types: Some services are offered by electronic registered investment advisers (e-RIAs) from online firms. In addition, some investment firms offer electronic advice options too, or they have partnered with e-RIAs under co-branding arrangements. *[See Finke-Cummings, page 43.]*
- Advice frequency: Some services provide ongoing advice, while others only set up the initial plan and still others provide for ad hoc advice such as upon first hire, start of pre-retirement period, etc.
- Advice scope: Some provide advice only on plan assets but others also advise on outside assets and even on broad retirement issues. Some connect participants with financial advisers too.
- Data handling: Some services allow plans to provide participant data to the automated systems, while others ask participants to enter personal information or to add information to that automatically provided by the plan sponsor. Participants may need to choose whether to store the data with the service, and if so, to elect password and other privacy options.
- Costs: Some services may cost less than comparable one-on-one advice, though not always. Costs vary between firms and also by services elected.

ADVICE DELIVERY PROFILE

Today's plan sponsors have many advice delivery choices. The options may include call centers, help desks, group seminars, one-on-one sessions, computer models, and brochures and other printed materials. (GAO 13-30, a 2013 report on 401(k) plans, p. 5)

KEY POSITIVES

- The automated systems can help keep advice costs low because the systems can be more efficient to replicate per employee advice versus one-on-one advice.
- Some systems may help improve investment—and retirement—outcomes. *[See Finke-Cummings, page 40.]*

ISSUES

- Computerized advice models vary considerably. This will make it necessary for plan sponsors to perform careful due diligence when comparing options. The Securities and Exchange Commission (SEC) and Financial Industry Regulatory Authority (FINRA) have published "Investor Alert: Automated Investment Tools" that may help in reviewing potential risks and limitations associated with these systems.
- Combination approaches are emerging. Plan sponsors need to ask if they can co-design blended approaches suited to their own plan environment. The following range of extremes shows some possibilities:

  General financial education... vs ...Personalized financial advice
  Investment-focused................ vs ....Retirement-focused
  On-going .... vs ....Ad hoc (event-based)
  Individually developed........... vs...... Technologically-developed
  Personal delivery..................... vs .... Online delivery

VARIETY OF DATA

Computerized advice systems use different types of personal data. In general, the more types of data, the more personalized the advice. But that varies, so ask what types and how many data points the participants can change to suit their particular circumstances. Some data types include:

- Age now, target retirement age, current salary and plan balance/allocation, spouse or partner, and other expected retirement income (most common)
- All qualified plan money, all personal funds and/or all household funds
- Retirement income goals, expected salary increases and expected annual rate of return (less common)
- Health status, mortgage and personal risk tolerance (rare, despite big impact on retirement)

[See Finke-Cummings, page 44.]

HELP IS AVAILABLE

The Society of Actuaries has published useful research on software development in this field.

Two reports in particular—“Retirement Planning Software” (2002) and “Retirement Planning Software and Post-Retirement Risks” (2009)—provide independent insight into issues and opportunities associated with these emerging retirement planning solutions. Both are good places to start when considering system capabilities and quality control issues as well as good places to return to for refreshers. For an overview of the 2009 report, check out these two additional files:

- “Retirement Planning Software and Post-retirement Risks: Executive Summary”
- “Retirement Planning Software and Post-retirement Risks: Highlights Report”

SOCIAL SECURITY ESTIMATES

If an automated system says it includes Social Security estimates in its recommendations, ask for examples. Society of Actuaries research has found accuracy varies between systems.

This is particularly important because Social Security is the largest source of retirement income for many households, yet many people start Social Security without understanding their options or the financial consequences of their decisions. In addition, many don’t realize that those estimates, even if accurate, do not encompass advice on which claiming strategy best fits the particular need.

SOME QUESTIONS TO ASK

- What help does a specific system offer–analysis, advice or both?
- What does the service cost, and who pays?
- What are the financial benefits and limits for plan sponsor and participants?
- Does the system include online help and 800-numbers for personalized assistance?
- Does the system integrate easily with face-to-face advice?
- How understandable is the output, especially for typical employees?
- How is data entered and stored (or re-entered if not stored)?
- How does the system handle privacy protection and quality control?
- If the systems provide recommendations, do they assume fiduciary liability for that?
- Do the systems incorporate statistically based modeling that includes a range of results or the likelihood that a specific participant will achieve a result?

9 How does one-on-one advice work?

Face-to-face advice has long been the traditional model for investment advice. However, the term "one-on-one" advice has gained traction in recent times. This refers to human advisers who provide personalized recommendations to plan participants.

The advisers perform this service not only in private meetings and communications with participants, but also in exchanges facilitated by technology (web chats, telephone, email, texting, etc.). The extent of the technology-enabled services depends on the service the plan sponsor has elected, and also on the willingness of the participants to use the technology.

Whether including technology support or not, a one-on-one advice service will provide the plan participant with the individual attention and recommendations of a credentialed adviser. But plan sponsors will need to know some things about advisers before making a choice.

TYPES OF ADVISERS

Not all advisers are alike. Some provide guidance to plan sponsors while others provide advice to plan participants. Some do both, especially if affiliated with a large professional practice or financial services provider.

In addition, some advisers are registered representatives and brokers who work through broker-dealers (which buy and sell securities). Others may be investment adviser representatives (IARs) who work through a registered investment adviser (RIA) firm (which also handles securities but operates under different rules than broker-dealers). Some may be dually registered, working as an IAR and also affiliated with a broker-dealer.

Dual-licensed advisers have both securities and insurance licenses. *[See Finke-Cummings, pages 7–15.]* Some may also be certified as financial planners, accountants or retirement professionals.

Because of this variety, advisers hold different types of licenses and professional certifications. They are often subject to differing governmental bodies, laws and regulations, too. And while some only provide advice, others provide education, guidance and advice. Some provide education and guidance but offer advice as an added service.

THE CHALLENGE OF ADVISER VARIETY

Those variations can impact outcomes in critical ways. Here are just two examples:

- **COMPENSATION:** Some advisers collect fees based on work provided or as a percentage of assets under management (AUM). Others are paid by commission, and some are compensated by both fees and commission.

  Plan sponsors need to be aware that the cost of advice services—or certain types of advice services—may be bundled into overall plan fees and charges or treated as an additional cost to the plan or as a cost to the participant. In addition, some firms that provide advice may have a financial interest in the outcome of the recommendations. Some of these factors can affect the actual return experienced by the plan participant.

  This raises important questions about cost disclosure. We will look at costs in greater detail later but for now, here are a couple of questions to keep in mind:

  - If paid by commission, might the adviser direct a plan participant to select the highest commissioned investment options when comparable options are available at lower cost? The DOL has expressed concern about this and has proposed a regulatory approach to address it.
  - If paid by fees, who pays—the employer or participant? Do the payers understand the potential impact—for instance, on costs or investment performance? Some plans pay the fees but allocate the costs to all participant accounts, often resulting in larger accounts paying more than smaller accounts and participants paying for services they do not use.

HOW FEES CAN IMPACT 401(k)s

Assume Jerry's current 401(k) account balance of $25,000 averages a 7 percent annual return until he retires 35 years later.

- If fees and expenses average 0.5 percent, his account balance 35 years later will be $227,000.
- If fees and expenses average 1.5 percent, his account balance in 35 years will be $163,000—28 percent less.

Source: DOL, A Look at 401(k) Plan Fees

- **STANDARD OF CARE.** This term refers to the duty of care under which the adviser operates. *[See Finke-Cummings, page 11–15.]* The plan sponsor needs to know the adviser's standard since this can impact outcomes. Here is a brief overview of the chief differences in the two prevailing standards:
  - The ***fiduciary standard*** requires an adviser to do what is in the client's best interest. This is often described as the most stringent standard, since it requires the adviser to put the client's interests ahead of the adviser's own interests, even if the recommendations will generate less income for the adviser and the adviser's firm. In the DC plan world, this standard currently applies to RIAs and their IARs who work with them. Larger RIAs are regulated by the SEC and smaller RIAs by their state securities regulator. Plan sponsors also have a fiduciary responsibility—for selecting and monitoring the advisers who have access to the participants.
  - The ***suitability standard*** requires the representative to provide investment advice that is suitable for the client's needs, goals and circumstances. The standard is viewed as less stringent, due to potential conflict-of-interest issues, such as the representative being able to recommend the highest commissioned investments even when less costly options are available that are also suitable. This standard currently applies to registered representatives of broker-dealers, insurance companies, banks and mutual funds. Broker-dealers and their representatives are regulated by FINRA. (Insurance agents also operate under the suitability standard.)

  PROPOSED CHANGES: Under current law, advisers who are subject to either standard may provide personalized investment advice to DC plan participants. 2015 proposed federal DOL regulations may alter that, but for now, plan sponsors need to be aware of the differences—and to remember that, as plan sponsors, they are fiduciaries for their company plans.

SOME QUESTIONS TO ASK

- How do the fiduciary standards that apply to the plan sponsor affect a decision to offer education, guidance and/or advice?
- To what standard of care does the advice-giver adhere?
- What impact will this standard have on our plan participants?
- How do we measure the impact and the quality of the service provided?
- How do we document and monitor the adviser's stated standard and regulatory compliance?

NECESSARY FIDUCIARY CHECK

- Under ERISA, the plan sponsor is automatically held to the fiduciary standard, but this is not automatically the case for those who provide advice or other services.
- Multiple sets of regulations affect this area and are in a state of flux, so specialized legal assistance is critical.

CHOOSING AN ADVISER

Plan sponsors have a fiduciary responsibility for selecting and monitoring advisers that have access to their plan participants through the plan itself. The decision to work with an adviser needs to be documented. A guidepost is the prudent investor rule, which is a widely recognized legal doctrine that establishes standards for managing investments. It requires those who make and implement investment management decisions to exercise the "care, skill and caution" as a prudent investor would do.

Plan sponsors who want to offer one-on-one advice in their plan will also want to ensure that the adviser will provide quality service. Think of it as another aspect of quality control.

As with any due-diligence process, the selection process will include background and reference checks on the advice service along with a review of key credentials and tests on the quality of advice in different situations. It is also important to establish a method of monitoring advice delivery, including reviews of the quality control processes of the organization itself.

A few words about adviser credentials:

- ***Licenses of advisers:*** Advisers can have one or more licenses. The common state licenses are for insurance and securities. Some states also have consultant licenses. The common federal licenses are Series 6 (for those selling "packaged" products like mutual funds and variable annuities) and Series 7 (for those selling most individual securities with a few exceptions). As noted earlier, RIAs are licensed by either the SEC or their state, depending on AUM. Advisers often have other licenses as well, such as in accounting and financial planning. *[See Finke-Cummings, page 46–48.]*
- ***Certifications and designations:*** Programs conferring certifications and designations vary in depth, experience and professional requirements, accreditation status, continuing education measures and other criteria. Two designations that focus on personal financial planning are certified financial planner (CFP); and, for those holding a certified public accounting license, the personal financial specialist (CPA/PFS). Three that focus on retirement planning are: certified retirement counselor (CRC), retirement income certified professional (RICP) and retirement management analyst (RMA). *[See Finke-Cummings, page 46–48.]* Other designations—such as the chartered financial analyst (CFA)—do exist, so it's worth taking time to research them. Some look-up options are shown in the toolbox.

TOOLBOX FOR ADVISER LOOK-UPS

These online tools can help locate advisers and research adviser credentials:

- BrokerCheck at FINRA
- CFP verification by the CFP Board
- CPAverify by National Association of State Boards of Accountancy (NASBA)
- Designation Check at the American College of Financial Services
- Professional designation search at FINRA
- Protect Your Money at SEC

Heads up: Tools and approaches that advisers use can impact recommendations. For instance, one software tool might require data about 40 or 50 different data points on each participant, while another might only request 10 or 15. The resulting computations could end up being quite different.

SOME QUESTIONS TO ASK

- How is the adviser regulated?
- What license(s) or certification(s) does the adviser have and are they current?
- If an investment adviser, is the advisers Form ADV up-to-date and provided with disclosure?
- Does the adviser check out with one or more of the look-up services in the toolbox on the previous page?
- How do the credentials pertain to the proposed delivery of advice?
- What are the sources of the adviser’s compensation, and is each disclosed to the participant?
- Does compensation change by products purchased, and if so, how and why?
- What do our participants need to know about this adviser?
- What automated tools does the adviser use?
- Do different advisers at the same firm provide the same or different advice?
- Will the firms offering advice provide examples based on “test cases” supplied to them?
- Can the adviser provide us with samples of his or her output?
- What control does the plan sponsor have over the advice-giving?
- Does the adviser’s firm have a strict quality control and compliance process?

SCOPE OF ADVICE SERVICES

The scope of service for investment advice is impacted not only by the experience and expertise of the adviser but also by many other factors—plan design, other plan options, access the adviser has to participants, desired cost structure, the participants' other financial issues (outside of the plan, like paying off the mortgage), and technology capabilities of both adviser and plan sponsor.

Whatever scope is agreed upon, it will be important to communicate that to plan participants. They will need this so they know what to anticipate when questions arise. This is especially important for near-retirees and retirees, many of whom may need investment and retirement advice frequently and may need reminders of what the advice service does and does not provide.

SOME QUESTIONS TO ASK

- With what types of decisions do we want to provide help?
- Does the proposed level of service meet the scope of services we want?
- Does the scope include the participant's total portfolio and total household?
- Can we negotiate the standard of care provided by the advice service?
- If the advice focuses solely on plan assets, how effective will this be in the long run?
- If the scope reaches to post-employment, what is the company's liability for that?
- If employees want additional services, can they buy them through the same source?

SCOPE OF SERVICES

The Certified Financial Planner Board of Standards Inc. publishes a list of Principal Topics, which might be included in the scope of services of an advice provider.

10 What are the cost issues?

Advice costs vary right along with plan design and size. Some of the many factors that affect cost follow. *[See Finke-Cummings, page 22.]* To learn more, it may help to check out DOL's report titled: *"A Look at 401(k) plan fees."*

- ***Adviser type:*** Fee-only financial advisers typically provide advice to individuals for an hourly fee, asset fee, or monthly or annual retainer. Managed account providers may charge annual asset fees (say, 0.15 percent to 0.5 percent of the retirement account assets), but a lower amount if advice services are provided to all employees. RIAs typically charge an asset fee or an hourly fee, and registered representatives and insurance agents typically receive product commissions.
  - *Ask questions:* Some advisers work on fees for certain services and/or commissions for others. Under current rules, advisers may or may not be held to a fiduciary standard; therefore, the plan sponsor needs to look carefully at who is offering what and why.
- ***Conflicts-of-interest:*** There are no conflict-free compensation models. This means it is critical for the plan sponsor to understand how the adviser is paid and how the adviser's compensation model can influence advice delivered to plan participants.
  - *Examples:* If paid by commission, an adviser may be incented to encourage more trades. If paid by fee (based on AUM, flat or hourly), the incentive may be to accumulate assets and disregard other issues such as paying down debt. If paid hourly, the incentive may be to work less efficiently. If paid on retainer, the incentive may be to work quickly and move on to the next customer. If paid by both fee and commission, the incentive may be to try to collect twice without disclosing such activity. *[See Finke-Cummings, page 34–39.]*
  - *Hot topic:* Regulators are concerned about rollovers from retirement plans and possible conflicts of interest in advice that participants receive. The DOL has proposed rules governing this area and the GAO issued a 2013 report on rollovers (GAO 13-30). DOL's proposed rules are not final, but they have already made financial and retirement advice into a major topic of public discussion.
- ***Plan size:*** Very large plans generally command more competitive pricing on advice services than small plans, especially when the services are offered to all employees. Or the large plans may be offered programs that provide several advice options at different price points (ad hoc, automated, face-to-face, etc.).
- ***Cost sharing:*** Some DC plans pay the cost for all participants. Others pay for certain levels of advice up to a maximum. Still others co-pay with participants or require participants to pay all.

CAUTION ON FEES

- When participants pay for their advice, the fee is generally in addition to the management fee for elected investments and sometimes a portion of the plan administrative fee too.
- The plan sponsor will need to exercise fiduciary-level care in assessing the impact of these costs.

- ***Provider type:*** The fee may vary by whether the provider is an insurance company or a mutual fund company.
- ***Big picture:*** Some fund options in a plan may cost 2 percent or more while others could be a fraction of 1 percent. When evaluating cost of advice, the plan sponsor will want to look at that. The sponsor may also want to explore how the adviser (or advice software) chooses funds to recommend, as the answer will provide a window into advice strategy. The strategy is important because it can impact overall plan cost and return to participants—and participants' satisfaction with the plan.

INVESTMENT EXPENSE RATIOS

Typical expense ratio ranges:

- 0.5 percent (50 basis points) to 2.5 percent for well-known or branded funds
- 5 to 15 basis points for passively managed funds
- 4 basis points or so for institutional class index funds

[See Finke-Cummings, page 38.]

SOME QUESTIONS TO ASK

- Have we evaluated conflicts-of-interest issues?
- What is the projected total cost of advice for, say a year, under the proposed program?
- Who pays the cost—the plan, the participants or a shared cost arrangement?
- If participants share, does the cost only apply to those who use the advice?
- Does the service allow payment on a per-event basis or must it be a recurring cost?
- How much experience does the provider have in costing-out the advice service it is offering?
- Is the cost of advice competitive with, or lower than, what the participant would pay at retail?
- Can the provider demonstrate a net improvement in results through use of the service?
- How much additional return is needed to show benefits from the result?
- For how long will the proposed cost for advice stay in force?

11 Do advice programs need monitoring?

To ensure compliance with stated objectives, plan sponsors will likely want to monitor ongoing use, performance and quality of their advice programs.

[See Finke-Cummings, page 52-53].

Plans of all sizes will probably be able to phase this monitoring into their quality control processes. Larger plans can probably do it themselves, but smaller and medium-sized plans may turn this function over to a qualified consulting firm. Either way, the cost will be minimal when compared to the potential expense of remedying problems that may arise if not monitored.

Some might include benchmark reviews at time of annual plan review to help spot possible areas for improvements or expansion. In large plans, quarterly reviews might help, say by running participant feedback polls on small segments of the population. Some plan sponsors might want to run test cases periodically.

SOME QUESTIONS TO ASK

- How many participants are using the advice?
- Have we tested and reviewed the advice that will be offered in specific situations?
- Have corrections from the last audit been completed?
- Does the adviser still meet the established criteria—licenses, certification, etc.?
- Does the adviser follow agreed-upon advice processes—assumptions, disclosures, reports, etc.?
- Have the recommendations remained free of bias toward highly compensated investments or certain parties (such as the plan provider)?
- What security measures does the adviser use to protect participant data?
- If the adviser is seeking a cost increase, what are the reasons and what is the likely impact?
- Should we put out a request for proposal (RFP) for a new adviser?

For a wide assortment of other questions and issues, see Finke-Cummings, page 56-60.

12 What might the advice choices look like?

What kind of advice choices might today's plan sponsors be considering? Though this varies by provider and market, the following chart shows some options that may be available to plans.

Advice Options

Type	How delivered	Provider	Compensation	Employer role
FEE-BASED	Employer pays fee to a qualified adviser to deliver advice to participants	Adviser chosen by participant	Employer pays part of adviser's fee and participant pays excess	Defines how much to pay, eligible group, services to be covered; pays fee
ONGOING	Advice firm provides ongoing advice as per agreement	Advice firm via advisers and technology	Varies: by group or per individual; can be fee, based on percent of AUM	Chooses adviser, sets scope, provides information, monitors quality, pays fee
EVENT-DRIVEN	Advice firm provides statements, seminars, individual counseling, etc. as needed	Advice firm via technology and advisers	Plan-set fee based on scope of service and headcount; service usually limited to plan options	Chooses adviser, sets scope, provides information, monitors quality, pays fee
PROVIDER	Mutual fund or insurer provides its own advice system –automated, face-to-face, or both	Mutual fund or insurer via technology and advisers	May be bundled with other services, or separate fee or commission	Defines elements of service in provider contract, provides information, monitors quality
THIRD PARTY	Third-party advice system, including managed accounts, primarily online with call center support	Third-party advice provider	Fee based on total population plus percent of assets for management of assets	Chooses firm, sets scope, provides information, monitors quality, pays fee not attached to managed account
AUTO	Automated system offers advice, without support from a human adviser	Third-party advice provider	Fee based on service and probably total population	Chooses service, provides information, monitors quality, pays fee

Source: Anna Rappaport, Anna Rappaport Consulting, Chicago
Note: Group purchasing arrangements are also available. In these approaches, the employer arranges for advice service at an attractive price, but plan participants pay for it on their own.

This expansion of choices comes at a good time. As noted earlier, retirement plan experts are becoming increasingly aware of plan participants' need for advice. This includes not only how to save and grow retirement funds—that is, investment advice—but also what to do about pre-retirement questions such as: When to retire? Where to live? When to claim Social Security? And what about other retirement living and financing issues?

Fortunately, government regulations impacting DC plans are changing in ways that make it more feasible than ever for retirement plans to offer advice programs in both areas.

The advice service arranged through a plan typically ends when the employee retires. However, a few advice providers now offer the opportunity for participants to transition over to a post-retirement advice program under a separate, retail market contract.

Since many people now live for 10 to 30 years after leaving work, and since the need for retirement advice may even increase in the post-work years, such transition opportunities appear to be a positive development. Participants don't have to accept the offer to continue with the service in the post-retirement years, but if the service is available, they may appreciate having the option.

Choice is a core concept in the advice environment now in the making. Employers can elect to offer advice programs or not; employees can elect to use those programs or not; and at retirement, retirees can—if plan design permits—elect to continue receiving advice services of the same provider, but on a retail basis. This is a perfect time for these options to become available, since the retirement security needs of Americans have never been greater, even as employers are greatly in need of high-value benefit programs that help recruit and retain employees.

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TOOLS

BrokerCheck, FINRA: http://brokercheck.finra.org/

CFP verification, CFP Board: http://www.cfp.net/utility/verify-an-individual-s-cfp-certification-and-background

CPAverify, National Association of State Boards of Accountancy (NASBA): https://www.cpaverify.org/

Designation Check, American College of Financial Services: http://www.designationcheck.com/advisor-search

Professional designation search, FINRA: http://www.finra.org/investors/professional-designations

Protect Your Money: Check Out Brokers and Investment Advisers, SEC: http://www.sec.gov/investor/brokers.htm

ACRONYMS

assets under management (AUM)

certified financial planner (CFP)

certified public accountant/personal financial specialist (CPA/PFS)

certified retirement counselor (CRC)

chartered financial analyst (CFA)

defined benefit (DB) plans

defined contribution (DC) plans

Department of Labor (DOL)

electronic registered investment adviser (e-RIA)

Employee Retirement Income Security Act (ERISA) of 1974

Financial Industry Regulatory Authority (FINRA)

Government Accountability Office (GAO)

investment adviser representative (IAR)

individual retirement account (IRA)

qualified default investment alternative (QDIA)

registered investment adviser (RIA)

retirement income certified professional (RICP)

retirement management analyst (RMA)

Securities and Exchange Commission (SEC)

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