

## Retirement

### The shaky state of retirement: be ready to help your clients find solid ground

BY ELIZABETH GALENTINE

**A**s Founder and President of the Retirement Learning Center and Executive Director of the PLANSPONSOR Institute, John Carl has his finger on the pulse of a host of issues facing the retirement industry. "It's really an interesting time," says the self-proclaimed "ERISA nerd." *EBA* caught up with Carl for a two-part chat about presidential policy initiatives and why now is the perfect time for health care consultants to dive into the retirement side of employee benefits.

#### How did the retirement market get to where it stands today?

The issues haven't changed, but the tactics from administration to administration have dramatically changed. And when I look back and I see the Pension Protection Act as the Bush administration's big approach to retirement, the Pension Protection Act essentially would be better named the Pension Destruction Act because it really increased risks and costs for running

corporate pensions in America, and we've seen a tremendous amount of freezing and termination of corporate pension plans since its enactment.

But that said, I think they knew that and what they were trying to do is create a systematic mark-to-market approach to valuing the true assets and liabilities of pension plans. Then of course the 2008 market came and we're back up to 12-year asset smoothing, it looks like.

I think they knew that the Pension Protection Act was probably going to be the death knell for most corporate pensions in America, or at least as the primary retirement plan. That's why the Pension Protection Act had so much about defined contribution plans in it. Because if you're going to make it difficult to run a corporate pension, then you're essentially acknowledging that Americans will retire in defined contribution plans.

#### How does that change the outlook?

There are three major problems with that. No. 1, it's voluntary, so you have a lack of participation. And that continues to be the major problem. I think the stats are that one-third of all Americans who are fortunate enough to be in a corporate DC plan with a match choose not to take the free money. And that's a problem. So if you're fortunate enough to be on the hallowed ground working at a company that's actually matching you, about one third of Americans do not participate and do not take the free money that's being offered to them.

So if we're shifting from a previously defined benefit retirement system to a defined contribution retirement system, you gotta fix that. Participation is a big problem.

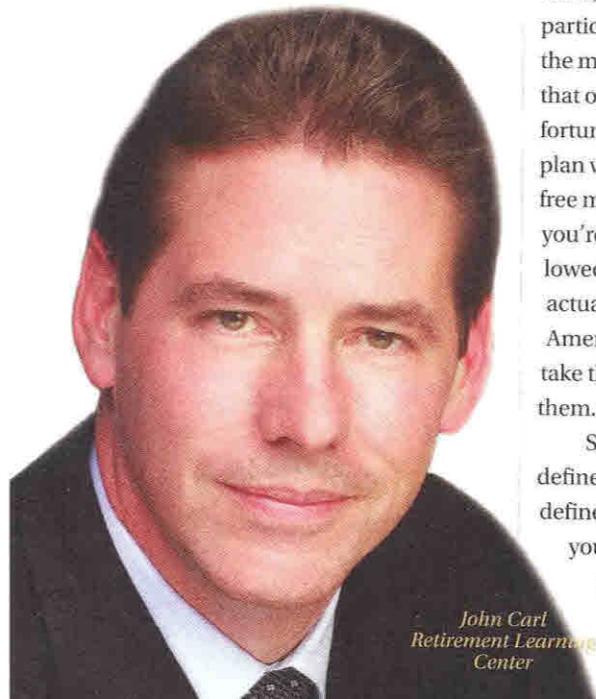
The second major issue is performance. Because most Americans, if they muster up the gumption to contribute to their 401(k) plan in this type of economy, they're probably not skilled investors and they're not going to get the type of investment returns that a professional investment management group supported by consultants is going to get. So performance in defined contribution plans tends to be the second issue.

The third issue is if you want to get it right and you're not a sophisticated, world-class investor, then you would probably seek some guidance or advice from a professional. The way that the laws are written right now, there's a huge disincentive for any firm or investment adviser to really offer advice because it makes you a fiduciary — which opens you up to lawsuits and personal asset liability for telling folks what to do.

So to me, the three things they had to address were participation, performance and advice. And the Pension Protection Act tried to do that in the previous administration by offering incentives to the business owners, to the corporations. They said, "If you automatically enroll everybody into a qualified default investment alternative, which is a QDIA, here's your big incentive: Anybody who sits in that QDIA asleep at the switch, they can't sue you. The Department of Labor will not recognize a lawsuit." That's a big class exemption.

#### What was the result?

So of course the industry rushed and created the easiest QDIA to implement, which is a target-date fund. All of these people ended up in target-date funds, which became the fastest growing mutual fund



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category in America, and of course as we saw the Senate Aging Committee take on, that didn't work out so well.

In 2008, I think the worst performing 2010 target-date fund for "Mrs. Lubner" in the mailroom who's supposed to retire on or around 2010, in 2008 she's down 43%. So Sen. Herb Kohl [(D-Wis.)] took on this issue as part of the Senate Special Committee on Aging. They held hearings and

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what essentially they found is that most of these 2010 target-date funds weren't really being run for 2010 retirement events. They were being run for the life expectancy of someone who's retiring in 2010.

So there was a joint task force being created between the Department of Labor and the SEC. They've released several findings thus far which essentially point the gun at the plan sponsor, saying, "You need to do prudent selection and ongoing monitoring of your target-date fund."

Unfortunately just about 85% of target-date funds are sitting either at Fidelity, Vanguard or T. Rowe Price. Not that they're bad firms or bad managers. They got there because those guys are the proprietary recordkeepers. That's not prudent selection, that's just taking the proprietary offering.

From the Pension Protection Act start, in this administration's agenda, target-date funds are a big focus. And any plan sponsor that has target-date funds had better be doing a good job of documenting how they prudently selected their target-date fund, or making a change if they haven't done that. And then [continue to] monitor to make sure that that's the right target-date fund for their makeup of their participant base.

### What do you think about advisers becoming fiduciaries?

I think it's a foregone conclusion. I think they already are, in almost all cases,

fiduciaries. Now there are a couple of different kinds of fiduciaries. There's the overall plan fiduciary who's involved in the total plan, the recordkeeping, the ongoing monitoring. I would call that a general fiduciary.

Then you can segment yourself and just be an investment fiduciary. But I think that in most cases advisers are acting as fiduciaries. I think unfortunately in most

cases their firms are trying to pretend that they're not.

I think if you're not going to be a fiduciary you're going to have a really tough time being an adviser in the retirement space. Because while target-date funds are a big issue, the other things that we talked about are how you address participation and performance and advice.

So what do we have going on right now? We have proposed regs from the Department of Labor on investment advice that are going to encompass not just retirement plan assets but also IRA assets. I think this is going to force the hand of broker-dealer firms to finally acknowledge that their people are giving advice on these retirement assets, and they're going to have to act in a fiduciary manner. The proposed regs say you either essentially act as an un-conflicted, level fee investment adviser, i.e. a fiduciary, or you act as a conflicted, unlevel fee advice provider. But then all of your advice has to be based on an independent third-party-audited computer model. And that doesn't sound like a very compelling value proposition if I'm a financial adviser.

So I think the Department of Labor and the Treasury are going to go forward and force the hand of firms and their advisers to acknowledge their fiduciary status on retirement assets. That's at least what the proposed regs would say. And we

would give that a high probability of going through.

### Is it dangerous for health advisers to dabble on the retirement side?

Well, they just have to understand that if they're going to play in this field the two questions are: Are you going to be doing institutional retirement plan work? And I would think most of your benefit advisers, that would probably be their natural client base, because they're doing the health care, maybe the P&C and the other benefits at the corporate level — which would give them access to doing retirement plans. So if they're going to do it themselves they're going to have to understand and act probably in a fiduciary manner in an environment with a whole lot more scrutiny.

Because the other stuff that's coming down the pike is there's been a major ramp-up in the enforcement side of the Department of Labor. They've added a tremendous amount of staff with the intent of enforcement. The DOL got 997 [new positions] in 2009 that they're still in the process of filling, and 70% of those are dedicated to enforcement.

They released what they call their 2009 "restoration results" from the EBSA, which of course is health care plans, welfare plans, retirement plans and all things under ERISA. They tagged businesses for \$1.36 billion in 2009 and they dramatically added to staff in the enforcement area. I think you're going to see the number of audits go up significantly and you're probably going to see the size of plans being audited come down.

So if your benefit advisers are going to go out there and personally get into the retirement space, you're going to have to have your "game on."

*Stay tuned for part two of our interview with Carl in October's EBA, in which he delves into how to be a high-quality fiduciary, as well as the Obama administration's ambitious efforts to keep retirement accounts afloat. EBA*