Episode 60

Hello and welcome to Revamping Retirement, a podcast brought to you by CAPTRUST, where we explore the opportunities and challenges facing today's retirement plan sponsors and fiduciaries. Our hosts, Jennifer Doss and Scott Matheson, lead the employer-sponsored retirement plan practice at CAPTRUST, one of the largest registered investment advisors in the U. S., and a thought leader in the retirement plan, advisory, and consulting space. We hope you enjoy Revamping Retirement.

Jennifer: Welcome, everyone, to a special episode of Revamping Retirement and the first one for 2024. I'm Jennifer Doss, and I have a few folks actually joining me today, which is what makes it special, to talk about our predictions for 2024 within defined contributions. First up, welcome back Audrey Wheat. As a reminder, Audrey heads our strategic vendor relations group, and she works really closely with all of our major recordkeeping partners on behalf of our clients.

Matt Patrick is also a returning host. He was just on one of the last episodes we had, and he leads our DC discretionary team that is now closing in on close to a hundred billion in assets. Congrats, Matt. And finally, we have a new host joining us, Pete Ruffell. So Pete leads our DC efforts for our large market and special projects team here at CAPTRUST.

So welcome, Pete. Do you want to take maybe just a few seconds to introduce yourself to the audience, a little bit about you?

Pete: Sure. Thanks, Jennifer. It is a pleasure to be here. Longtime listener, first-time caller. As Jennifer mentioned, my name is Peter Ruffell. I've been with CAPTRUST for 12 years. I'm one of the senior managers for our defined contribution team. And my primary scope is helping shape and develop our 321 fiduciary services.

Jennifer: Pete is also getting ready to have a baby at the end of this month. He's—we're just lucky to have his headspace right now. So appreciated.

Matt: 321 expert, soon-to-be father, and kombucha lover. That's what we know about Pete. Facts. All facts.

Jennifer: True. All right. I'm excited to hear what all of you have to say about 2024, as predictions are hard and if you don't get these right, you're just not going to be allowed back on the podcast. This is—it's a big deal. Just kidding. So to start out, Audrey, I'm going to come to you first. So give us your best prediction for 2024.

Audrey: Absolutely. I actually came prepared with two predictions. So hopefully I'll be right on one of these. Just to set the stage here, I lead our strategic vendor relations here at CAPTRUST. So what that means is the majority of my day-to-day is spent meeting with and conducting due diligence with our recordkeeper partners.

OK, so first prediction is that the recordkeeper consolidation and outsourcing trend will continue. The primary reason for this trend is due to recordkeepers' margins being razor thin, and one way to combat shrinking margins is to consolidate in pursuit of achieving scale. We've seen this time and time again over the years.

A lot of our plan sponsors that are listening to this podcast may have experienced a recordkeeper consolidation. There used to actually be about 400 recordkeepers around 15 years ago. And now we sit right around 100.

There is a newer trend where recordkeepers are outsourcing various parts of their operations to third parties. So you may hear recordkeepers referring to this as partnering.

Audrey: This trend can take shape in many ways. So some recordkeepers have elected to move virtually all operations and the people in those types of roles to an outside party, and just keep the face of their business as their brand name. Others have moved just a few areas of their business to the other firm, but opted to keep more of their people in house.

All right, so we've set the stage talking about the thin recordkeeper margins. So this brings us to the second prediction: Even after consolidation and outsourcing, the recordkeepers still have to find a way to meet their bottom line. So in order to remain viable in the business, most, if not all recordkeepers will need to have a standard side hustle to generate revenue. This is most often taking shape by offering products and services to plan sponsors within and outside the plan. Solutions like managed accounts, participant advice, HSA, and student debt solutions, to name a few. So if you're overwhelmed by this, of course, your advisor can help you sift through all these solutions.

Matt: Audrey, could you walk through, you laid out like a full recordkeeper acquisition versus outsourcing? Could you maybe walk through like, which one of those do you view as more likely? And then, I guess, which one of them is the most disruptive from the plan sponsor's end?

Audrey: It's a great question, and like any great answer in the financial realm, it depends. I can tell you that with traditional consolidation or one company acquiring another, we typically know how that goes. There's a whole communication strategy behind it. The plans migrate over to the new recordkeeper in waves.

It just depends on how many waves there are. And we really kind of know what to expect. It typically doesn't drag on for longer than a year or a little more, and then it's done, right? With the outsourcing, each recordkeeper that is bringing on third parties is really kind of blazing their own trail with outsourcing.

So it really depends on how disruptive it is, and also the timelines can vary—wildly. We've seen where in a year, the pain is over. And then we have some that have dragged on for years and years as they continue to kind of figure out what their offering looks like. So I would say that it's just easier to know what to expect with the traditional consolidation, but with the outsourcing, it's hard to know what's coming because we've not been through this before.

Matt:: And are they, are they outsourcing to similar providers on the back end or is it a wide range of people there?

Audrey: Yeah, we have seen a wide variety. We've seen some outsourcing to partners that they already have in place. So essentially just offloading tasks onto that partner that are new to that partner, but they have an existing relationship. We've seen others that bring on an entirely new partner that's relatively unheard of in the retirement plan recordkeeping space and try to kind of build an entire new offering with that provider. So again, it depends.

Jennifer: Audrey's not answering any of your questions.

Pete: But she's skillfully navigating around them and not mentioning any names all the while.

Audrey: Lips are sealed.

Jennifer: She's good at that. Well, Audrey cheated and brought two. So that's a lot of pressure for you, Pete, especially your first time on the podcast, 'cause I'm coming to you next. So it better be a good one worth two. So give me your prediction for 2024.

Matt: All right. So my prediction for 2024 is that cybersecurity will become a more normalized part of planned fiduciaries' annual procedures. If you can't seem to keep the year straight anymore, like myself, the DOL initially issued their guidance on this topic back in 2021. It ended up looking more like a list of best practices than guidance.

And those best practices came in three forms. They were tips for hiring a service provider with a strong cybersecurity practice; an outline of a strong cybersecurity program for service providers; and online security account tips for participants to reduce risk of fraud. And that was an interesting one, certainly, having the DOL talk to participants.

Why I think it's going to get more limelight is a function of what else has been on everyone's plates. Looking back: Secure 1.0 in 2019, COVID, retirement income, 2020, 2021. Secure Act 2.0 in 2022. Certainly that has taken the lion's share of the attention for our industry, but now with the combination of the DOL asking questions related to cybersecurity policies and procedures, the introduction of AI to mainstage society, and not to mention plan litigation on the rise related to fraud and account theft, you're ripening the reality that plan fiduciaries need to deliberately fold in this responsibility more wholeheartedly.

Since the released best practices, the DOL's poster child plan fiduciary is likely one that has regularly requested their service providers' answers. So the questions provided in the guidance reviewed and evaluated those responses as a committee and likely also included those questions as part of an RFP to consider alternative service providers.

My assumption is that many plan sponsors are still determining how best to tackle this endeavor. Questions like, is their recordkeeper going to have an expert join them, join a meeting to present on the topic? Are they looking to their investment consultant or their ERISA counsel to formulate a process? Do we have an IT professional on staff that can help us review an SOC report from one of our providers?

So by this year, my prediction is that many more plan sponsors will have fleshed out these types of questions and have established some expectations on how they will tackle this going forward. And I mentioned a quick acronym there, SOC report. Uh, what that stands for is systems and organization controls. What that is, is an internal—and also a SOC2 report, if we're getting into the details, will be an external audit of that—but an evaluation of internal control procedures, really to mitigate risk.

As a quick sidebar to this prediction, I enjoyed thoroughly watching my dad's frustration over the holidays as he repeatedly locked himself out of his 401k. Multifactor authentication will take some time getting used to.

Jennifer: All right. Matt, you have to round it out, and Pete just had a really sexy one. So I hope you brought the heat here. What's your prediction for 2024?

Matt: In Pete's shadow—and unlike Audrey, I'm going to meet expectations with one prediction as opposed to going above and beyond. I'm going to drift over to the investment side more so. And my prediction for the year is that we are going to have more conversations around custom QDIA solutions. And when I refer to custom in this context, I mean more customization on the participant level.

If you look historically within the defined contribution space, custom target dates have been around for a long time, and generally those are structured where you as the plan sponsor can select the underlying strategies, the underlying investments, and even the glide path for that structure. And that has some appeal if you have really strong views or you have a specific lean, or you want to intentionally leave some part of the investment realm out of your target eight series, but for the vast majority of plan sponsors, they're happy to go with an off-the-shelf product from a Vanguard, a T. Rowe Price, a Fidelity, a BlackRock, and so on.

So that's where the majority of assets have been. And that's the area that continues to grow the most, moving forward. In terms of customization, again, it's not a brand new idea. Products called managed accounts have been around for many years and are starting to pick up some steam. And that's more in line with this customization at the participant level.

So if you're not familiar with what the term "managed account" typically means, it's a service that is provided, and it looks at each individual within the plan and tries to take in as much of their data as possible: their age, their salary, their gender, what their savings rate is, and tries to get a better look at their financial picture overall so they can give them customized advice and also custom asset allocation—typically using the funds that are in your retirement plan today and allocating across those. And they're interesting services, because beyond just the data it can get from the plan's recordkeeper, it allows for participants to engage with the tool. They can put in savings goals, what they want to plan for. Do they need to account for health costs down the road? Do they need to save for students' higher education needs? And so it can really get you more tailored advice in a pretty cost-effective way within the plan.

So those are starting to pick up momentum, mainly because as they've been around and they've picked up assets and the technology has gotten a little better, the cost has come down 'cause they were a little expensive when they first rolled out, which caused some people to shy away from 'em. But that's coming down, and because they're starting to gain in popularity, we're starting to see variants of that come into the market. So if you have managed accounts within there that are the most customized, we're starting to see people come out with products that are somewhat in between a target date and a managed account.

And that's the trend that we're seeing, is edging closer and closer toward that full-on customization, but maybe creating some stepping stones along the way. So we see asset managers and recordkeepers that are starting to roll out products that either leverage an existing target date series or leverage the underlying components of a target date series.

And again, take in some data points on the individual and try to give them that something a little more customized than the vintage structure that target dates offer. So if you look at someone and say they're In the 2040 vintage, but really the best allocation for them would be somewhere between the 2035 and the 2040. These are the types of solutions that are coming to market, where they can say for you, Jennifer, or you, Audrey, or you, Pete, this is what your financial situation looks like. And this is exactly how much equity you should have. And that's between these two vintages. That, in addition to just ongoing pressure to add managed accounts out there and inclination from service providers to add those.

I think plan sponsors are just going to hear more and more about these. They're going to be pitched to them because it really does—it involves your recordkeepers, asset managers, and even consultants out there have these types of products. So I'd imagine it's something you'll hear about more, might even be pitched on it in the coming years, and something certainly that all plan sponsors are probably going to have to consider one way or the other moving forward.

Jennifer: it's really interesting, because we're actually, if you think about it, we're getting close to 20 years since the Pension Protection Act and when Targeted Aid funds really started taking off as the QDIA. And if you think about technology 20 years ago, we've got a lot more than we had back then and it does feel like there's an opportunity here to leverage what we have built as an industry, to offer something better and really go that 2.0.

Matt: It feels like it's time, yeah, the efficiency is really there in a way that it hasn't been in the past. So look out for all that. So that's my prediction. And I think, Jennifer, I don't know that we can let you escape without making a prediction. What are you seeing for the year upcoming?

Jennifer: Yeah, I didn't think you would. I have one. My prediction for 2024 is—it's not a fun one, but I have one—it's regulation and basically more regulation. I think that the

Department of Labor and the IRS are going to be extremely busy this year, responding to Secure Act 2.0 requirements, things that were just legislatively required for them to do by a certain date and also providing guidance on.

Some of those provisions that are already in effect or that just went into effect, January this year. From the Department of Labor standpoint, they're going to be really busy with the retirement security rule they proposed last fall, which is really what you'll hear people referring to as the fiduciary rule, or Fiduciary Rule 2.0 or 4.0, depending upon how people are talking about it. That rule would really update the definition of investment advice under ERISA and probably have the greatest impact really, in terms of a planned sponsor or planned participant experience on rollover transactions. So I'm not going to get into that on this, That would be a whole different podcast, but that's going to take up a lot of their time.

They also have to launch the participant lost and found database that was directed by Secure 2.0 by December 29 of this year. So very specific. The goal of that database—this is a reminder—is to allow terminated participants to be able to search and locate their retirement benefits. And the database is supposed to include contact information for plan administrators, which is going to assist people to be able to locate things, particularly tracking changes. If there's been plan mergers or divisions, bankruptcy, plan, consolidation terminations, plan name changes, basic stuff like that—that makes it very difficult to keep up with where maybe you have your money out there.

I would say the Department of Labor, they're also interested in providing guidance around emergency savings accounts this year. That's a big initiative. And they're also directed per SECURE legislation to focus on increasing the efficiency of participant disclosures. They did already issue an RFI in late 2023 that was focused on asking some questions related to fee disclosure improvements and how they could consolidate DC plan notices.

So they're already thinking about it. They're also directed on Secure 2.0, just to put another thing on the plate, to update the two safe harbor regulations that are related to electronic disclosure by the end of this year. Those updates are really required to account for the new requirement that will happen in 2026 that participants are going to have to receive at least one paper benefit statement per year, unless they qualify for an exception. So we really haven't talked too much about that one, but out of the 90-plus provisions, that was one of the ones that people weren't super excited about, but you eat your vegetables with your meal.

Moving on to the IRS, I would say they're also going to be really busy in 2024, despite that recent grab bag, or what people would call a grab bag of guidance that they issued in late December on a number of topics. that grab bag had things in it: guidance on Roth employer contributions, had de minimis financial incentives in there that were really topical. They're also expected to issue guidance this year on student loan matching and some further guidance on Roth catchups that they delayed enforcement on earlier this year. Also expected to finalize rules related to the timing and use of planned forfeitures, and some more guidance coming out for long-term, part-time employees, although what we have today from them is pretty solid and is being relied upon by people, but, they'll be finalized this year.

And then I'm actually going to throw in one legislative item too. I'm not going to count this as a second prediction. I'm not going to cheat like Audrey. This is all related. I have high hopes for legislation to be passed this year to allow CITs in 43B plans. I think it's time. I think it's always been a matter of when and not if, and unfortunately, it's a small thing that's going to need to be attached to a larger banking bill, but there's a bill that's already been introduced in the House. We expect a companion bill to be introduced in the Senate. So I'm keeping my fingers crossed for this one to, I think, finally get over the goal line in 2024. So that's my prediction for this year.

Matt: I don't know. That felt like cheating to me.

Jennifer: No, it was related. It's all government, All right. Now that everybody's predictions are out there, does anybody want to jump ship from their own and attach themselves to somebody else's that was better? Now's your opportunity.

Audrey: I just nominate that we regroup December 31, and we need to hold ourselves accountable. We need to figure out which ones came true.

Jennifer: All right, that'll be right around end-of-year review time. So I think that's good timing. Just all regroup and we'll have a conversation. So that's great, Audrey. Thank you all for joining me today. I really appreciate having you all here and getting your different perspectives and getting your predictions for 2024.

Thank you, everyone, for tuning in again to Revamping Retirement. Thanks for listening. You will be hearing from each of these individuals more throughout 2024. As a reminder, don't forget to subscribe to this podcast wherever you do get your podcasts, and we'll see you all next time.