



# The Future of DC: Personalized Investing

The Past, Present and Future of Professionally Managed Portfolios  
for Defined Contribution Plans

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## Executive Summary

This paper highlights the trends and evolution of multi-asset portfolio solutions in the defined contribution (DC) space, particularly Target Date Funds (TDFs) and Managed Accounts. TDFs have largely dominated as the Qualified Default Investment Alternatives (QDIA) in DC plans, offering professional management of age-appropriate portfolios at a reasonable cost. Discretionary Managed Accounts, despite superior personalization and open architecture design, have thus far failed to succeed as a QDIA solution, largely due to higher fees charged to defaulted participants who do not reliably engage to unlock the benefits of customization.

But that's beginning to change. We believe the future of DC will increasingly be defined by personalized investing, whereby the boundaries separating TDFs and managed accounts will fall away.

We believe these emerging innovations will amplify demand for and market share of managed account-powered solutions as retirement plans and their participants demand more personalized portfolio solutions.

- **QDIA Model Portfolios** leverage a managed account chassis to create personalized model portfolios, not at the participant level but at the plan level, akin to custom target date funds (CTDFs) but without the costs and operational requirements associated with striking a net asset value (NAV) at each fund. This provides plan sponsors of any size the ability to easily customize the number and spacing of portfolio vintages, asset allocation glidepath, vehicle type, asset classes and active/passive mix in a manner better aligned with plan demographics and sponsor preferences. Importantly, we anticipate QDIA model portfolios will not only be offered at no additional cost to the plan sponsor, but also include additional discounted fees for recordkeeping services, provided these solutions also incorporate the stable value and other proprietary offerings affiliated with the recordkeeper. Moreover, they could easily integrate recordkeeper data to reflect differences among participants across income, savings rate, account values, etc., to personalize portfolios without any participant engagement.
- **Personalized TDFs**. The same is equally true for Personalized TDFs, whereby a managed account chassis would use the same participant demographic information, namely income, savings rate, plan balance, etc., to enhance participant assignment and allocation to a TDF vintage portfolio(s) based on more than age alone. Arguably, both QDIA Model Portfolios and Personalized TDFs are poised to better facilitate a Hybrid QDIA experience, whereby participants would be seamlessly transitioned into a full-fledged managed account portfolio the moment they engage to volunteer additional datapoints related to their financial circumstances, goals and retirement intentions.
- **Advisor Managed Accounts**. New business models are emerging whereby the investment fiduciary's role may be altered and/or altogether subsumed by an unrelated third-party consultant, investment advisor or plan sponsor willing to serve as the fiduciary with investment discretion for the managed account and/or QDIA model portfolios. We expect AMA solutions may permission the ability for advisors to impact a wide array of variables and assumptions that drive the way these solutions work, from capital market assumptions to the asset allocation glidepath and underlying portfolio structure. AMA is uniquely positioned to not only tailor investments to better meet plan sponsor needs and preferences, but also amplify the role and value of the advisor, who will increasingly provide advice not just at the plan but also the participant-level, democratizing the availability of advice on not just investments, but also savings strategies, retirement age, social security claiming strategies and withdrawal strategies to a broader range of participants.
- **LifeTime Income Solutions**. With the recent passage of the Secure Act in 2022, innovation in the decumulation and lifetime income space has been turbo-charged. The key enabler of these solutions will likely be TDFs and managed accounts, with plan participants benefiting from the purchase of annuities to protect against the combination of uncooperative investment markets and long life. The benefits of the incorporation of annuities in professionally managed portfolio solutions range from the use of third-party financial experts overseeing the selection, negotiation and monitoring of the specific annuity product and insurance providers, determining how much to annuitize and how to modify corresponding portfolio allocations to leveraging the pooling of participant assets to do so on more advantageous terms than available in the retail market.

# Historical Issues Hampering DC Plan Success

## Rise of the 401(k) and Participant-Directed Retirement Plans

At their genesis, 401(k) and other DC plans were likely not envisioned to be the principal means by which Americans save and invest for retirement. Certainly, their cost, design and use would not lead to that conclusion, even several decades after they launched following the passage of the Employee Retirement Income Security Act (ERISA) in 1974 and the Revenue Act in 1978. With the continued decline of defined benefit (DB) pension plans as workers' primary source of retirement income – active DB participants have declined from a peak of 30 million in 1980 to just 12 million in 2020 – DC plans have become the primary retirement saving vehicle for Americans, as well as a vital complement to Social Security income, particularly within the private sector. The big problem was and remains that most individuals know little about how to save, invest, and plan for a successful retirement, as the vast majority of plan participants are not investment professionals, but were treated overnight as if they were. By the late 1990s and early 2000s, it became increasingly clear that many employees would simply fail to take appropriate, proactive measures on their own to enroll in their employer-sponsored DC plans, save an adequate amount of their paycheck, or invest in a diversified portfolio appropriate for their age and financial circumstances.

## Pension Protection Act and Improved Plan Design

In passing the Pension Protection Act (PPA) in 2006, Congress acknowledged both the rising importance of DC plans in enabling workers to maintain their lifestyle in retirement and the issues endemic to participant-directed retirement plan schemes, namely the lack of time, interest, or ability on the part of most participants to manage their investments and retirement objectives on their own. The PPA addressed many of these issues by using safe harbors to encourage plan sponsors to improve plan design through a smart combination of automation and defaults, including auto-enrollment of new hires at a pre-established saving rate, default investment in professionally managed target date portfolios aligned with investor age, and automatic escalation of deferrals over time.

## Transitioning from Accumulation to Decumulation

While these changes represent order-of-magnitude improvements in plan design and participant outcomes, much work remains, with most retirement plans and their participants in need of help, especially with respect to planning for retirement and the transition to decumulation. In the next section, we will review the evolution of target date and managed account solutions, with a careful examination of present-day deficits and opportunities for improvement. Finally, we will cover current innovations playing out across target date, managed account and guaranteed income solutions, all of which are extremely promising in addressing material investment and financial planning gaps and better living up to the goals of ERISA and a more secure income in retirement.

# Evolving Landscape for Multi-Asset Solutions in DC

## Target Date Funds (TDFs)

### Dominance of TDFs as the Default of Choice

Under the PPA, three types of investments qualify for use as a default investment for employees automatically enrolled in a 401(k) plan under the Qualified Default Investment Alternative (QDIA) provision: balanced funds, TDFs, and managed accounts. While all three options bring professional investment management to DC plan participants, TDFs are overwhelmingly selected as the QDIA by most plans today, accounting for more than 98% of all such plan sponsor elections<sup>1</sup>. The decision not to use balanced funds (and their closely related cousin, target risk funds) as the plan's default investment is readily intuitive. While they represented the first such instance of professionally managed multi-asset solutions in DC, their static asset allocation policy, typically 60% stocks and 40% bonds, fails to meet the diverse and changing needs of plan participants as they age and approach retirement. With respect to managed accounts, despite advantages in their open-

<sup>1</sup> Vanguard: How America Saves 2023.

architecture design and personalization capabilities, the lack of engagement from most plan participants and especially higher cost is, in our view, the largest driver of TDF dominance as the QDIA. TDFs not only bring professional management of age-appropriate portfolios at a reasonable cost to participants, but they were specifically designed for individuals defaulted into a plan without proactively initiating any action on their own. Most participants stay enrolled at a plan's established default rate and in the plan's designated default investment, with the notable exception of older participants closer to retirement.

### **Asset Allocation Enhancements**

This is not to say that TDFs are perfect – in fact, while target date solutions have come a long way since they were first launched by Barclays Global Investors (now part of BlackRock) in the 1990s, the need for further enhancement remains. When first launched, many TDF solutions had overly conservative asset allocation policies relative to today's practices, with most equity allocations beginning in the 80% range. Most all solutions available today have re-risked, adopting higher equity allocations for longer, with initial equity allocations for investors in their 20s typically beginning in the low to high 90% levels and often staying there until investors enter their 40s and are less than 25 years from their expected retirement. We believe the more aggressive equity allocation glidepaths are generally more appropriate given investment horizons of 60 years or more and inadequate participant deferral levels. TDFs have also improved portfolio diversification relative to decades past, with higher allocations to foreign developed and emerging markets within equities as well as to Treasury inflation-protected securities (TIPS) and global/credit-oriented strategies within fixed income. Nonetheless, inflationary shocks experienced following the pandemic and unprecedented monetary and fiscal intervention exposed weakness in portfolio design. We would like to see incorporation of additional real asset strategies to improve portfolio resiliency in the face of inflation.

### **Other Portfolio Improvements**

Despite a strong track record of asset allocation improvements over the years, TDFs have been and remain deeply proprietary in design, though even this is beginning to change on the margin. Historically, asset managers best positioned to capitalize on QDIA opportunities were large fund families – especially those affiliated with recordkeepers – with the product breadth and quality needed to create well-diversified, high-quality, low-cost multi-asset portfolios. In fact, as of 2022, seven of the top ten TDF providers are asset managers affiliated with recordkeepers, accounting for a whopping 77% market share.<sup>2</sup> Still, many initial TDFs suffered from excessive manager concentration risk, with high allocations to individual strategies in core asset classes like domestic large-cap equities and core fixed income. This has been partially addressed through the incorporation of additional strategies managed by different portfolio management teams within the same fund family, though in many cases the core research platforms driving issuer selection within equities and fixed income remain much the same.

### **Custom Target Date Funds (CTDFs)**

In creating and managing institutional portfolios, we believe it's safe to say this level of concentration within one fund family is universally avoided by institutional investors, who seek to build more diversified investment portfolios featuring the highest quality managers within each asset class. The desire to improve portfolio diversity, reduce manager concentration risk and better account for other plan benefits that materially impact participant demography relative to the broader DC industry have led many of the mega retirement plans (generally those with more than \$1 billion in plan assets) to implement CTDFs. These plan sponsors generally sponsor multiple retirement plans in a single master trust with assets held by a large custodial bank, providing the opportunity to create white labeled funds unitized across multiple retirement plans. These CTDFs represented the first such instance of TDFs which blended active and passive investment strategies, a mix of mutual funds, separate accounts and collective investment trusts (CITs), and an asset allocation glidepath customized to better account for the presence of a DB pension and other plan sponsor benefits.

### **The Impact of Indexing and CITs on Fees and Product Design**

Dominant and growing market share gains from passive target date fund families like Vanguard, BlackRock, State Street and Fidelity, in addition to increased adoption of CITs, have amplified fee compression trends within the target date market, with

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<sup>2</sup> Morningstar: Target-Date Strategy Landscape: 2023.

overall pricing falling by roughly half over the past decade, declining from an average of 0.60% in 2013 to 0.32% in 2022.<sup>3</sup> CITs offer not only the same market liquidity features and scale economy benefits as mutual funds, namely daily trading on a post-notification basis with investors owning units of a commingled vehicle, but also the added benefits of pricing and investment flexibility. With respect to pricing, CITs can offer different share classes just like a mutual fund, but unlike mutual funds, they can be offered in a gross-of-management fee share class. This feature enables TDF managers to separately price larger-sized opportunities in a manner consistent with institutional separate accounts, as well as to set the price at the fund-of-fund level (as opposed to the weighted average of underlying acquired fund fee expenses (AFFE)), enabling flat and more consistent pricing (referred to as unitary pricing) across all target date vintages.

From an investment perspective, the CIT format also permits unlimited investment in third-party investment strategies in a manner that mutual funds are prohibited from so doing. This, along with the desire to arrest or at least slow the continued market share gains of low-cost passive TDFs incented most active TDF families to also launch active/passive blended solutions. This not only resulted in the halving of fees relative to their active target date counterparts, but also reduced manager/strategy concentration risk and introduced opportunities to better complete portfolios with passive exposure when internal active management capabilities were lacking. Similarly, it has also opened the door to what is referred to as “co-manufactured” opportunities with recordkeepers in which the TDF solution incorporates an allocation to the stable value strategy affiliated with the recordkeeper to reduce duration risk within the fixed income sleeve, provide the recordkeeper economic participation within the solution while reducing AFFE, and provide plan sponsors within the advisor-sold channel (generally plans of less than \$25 million in assets) credits and rebates to offset recordkeeper costs. With all of these benefits, CIT market share has dramatically increased, growing from 19% of 401(K) plan assets in 2011 to 33% in 2020 and more than quadrupling overall assets from \$370 billion to \$1.76 trillion in 2020.<sup>4</sup> This is especially true within TDFs, with CITs now accounting for 47% market share, and rapidly growing, especially within larger retirement plans.<sup>5</sup>

## Discretionary Managed Accounts

### The DOL SunAmerica Advisory Opinion and Birth of Managed Accounts

While managed accounts were launched in the early 1990s, they had minimal plan sponsor adoption until the Department of Labor (DOL) issued the SunAmerica Advisory Opinion in 2001 – a transformative event for bringing customized multi-asset model portfolio solutions to retirement plans, providing clear and explicit means for addressing conflicts of interest arising from portfolio allocations to investments affiliated with the plan recordkeeper. As a result, plan participants could now receive portfolios customized based not only on their age, but also financial circumstances and risk tolerance driven entirely through computer-based algorithms. Plan adoption was further aided by the passage of the PPA in 2006 and its corresponding eligibility to serve as the plan default, providing a strong “endorsement effect.” As a result, availability of managed accounts in DC plans grew from 6% of plans in 2005 to 59% of plans in 2019. We anticipate this trend to continue, likely eclipsing an 80% adoption level before 2030. During this same period, overall managed account assets have more than doubled, growing from \$108 billion in 2012 to \$271 billion in 2020, but have only increased market share of plan assets from 2.9% to 3.6%, according to Cerulli. If we adjust this to account only for the 59% of plans that have currently adopted managed accounts, this implies market share of just over 6% of plan assets. We believe the market share of plan assets will increase as pricing differentials relative to TDFs compress and as participant populations age, increasing the need for advice.

### Personalization

Managed accounts have long delivered superior personalization to plan participants relative to TDFs in that portfolios are customized on more than just age alone, but also on a wide range of other important factors that determine portfolio suitability, including:

- Risk tolerance and a participant’s overall comfort with risk and large changes in their account value

<sup>3</sup> Morningstar: Target-Date Strategy Landscape: 2023.

<sup>4</sup> Morningstar: Retirement Plan Landscape Report: 2022.

<sup>5</sup> Morningstar: Target-Date Strategy Landscape: 2023.

- Investment horizon, including not just age but also expected retirement date and mortality
- Account balance, including loans and especially assets held in external accounts
- Social Security, annuities, defined benefit pension and other plan benefits
- Salary and contributions: salary, employee deferrals, and employer match
- Spending needs in retirement, typically defined as an income replacement ratio
- Spousal considerations

Initial implementations typically did not capture dynamic feeds from third party financial institutions and were instead manually entered by participants – today, account values and corresponding investments held in outside accounts are often linked by participants and fed dynamically to managed account solutions via Yodlee, Plaid and other account aggregation services. This allows managed account services to account for fluctuations in the total market value of retirement savings daily, enabling better alignment of investment portfolios, as well as saving and retirement age advice with investor goals and objectives.

## Portfolio Design

Portfolio design for most managed account solutions leverages the same lifecycle finance concepts as TDFs, with younger investors with long investment horizons, little financial capital and significant human capital (as represented by the net present value of future earnings) invested in equity-heavy portfolios and older investors closer to retirement invested in more conservative investment portfolios with higher fixed income allocations. Managed accounts go quite a bit further to personalize portfolio allocations, accounting for differences among similar-aged investors across the factors discussed earlier, namely savings rates, account values, income levels, investment horizons and the like. This explains the generally higher uptake of managed accounts by progressively older investors, all of whom become increasingly heterogeneous precisely as they near the end of their working career and need more advice regarding their overall retirement readiness and retirement income strategies.

Managed accounts are open architecture by design in that they typically use the same investments offered to participants within the plan lineup. We would argue that this provides the benefit of oversight by independent fiduciaries charged to select investments needed to build a well-diversified portfolio that are also in the strict best interest of participants. Since most plan lineups are curated to not overwhelm participants with too much choice, managed accounts typically incorporate fewer dedicated asset class exposures and investment strategies than TDFs but remain comparably diversified across broadly defined asset classes. But even this is beginning to change, with plan sponsors increasingly able to preserve the plan lineup design for participants, while offering managed account providers the ability to use non-plan investments to further diversify and augment the core lineup, even utilizing 100% non-plan investments should they choose to do so.

## Advice

The advisory capabilities embedded within managed accounts are quickly improving, moving beyond investment allocation and savings advice alone to retirement age advice, Social Security-claiming advice, and withdrawal advice — including when to drawdown savings, from which accounts and, in short order, whether and how much to annuitize. Even accumulation advice is getting an upgrade. While a top goal remains getting participants to start saving more earlier in life such that income deferrals exceed 10% by age 30 for example, increasingly accumulation advice will also include which plan sources to invest in, from traditional to Roth or after-tax, and when. Comprehensive advice is a key differentiator of managed accounts, helping participants know how much to save, how to invest, when to retire, how much to spend and from which accounts.

## Pricing

In the early 2000s, managed accounts were initially offered at 100 basis points (bp) or 1% of account assets. While this pricing remains commonplace in wealth management today, the wealth management client typically has customized financial planning covering their entire financial life, not just retirement plan assets, and in-person meetings with a dedicated financial advisor. Not surprisingly, as target date pricing continues to compress, so it has for managed accounts, with pricing today typically starting at 60 bps and declining to 45 bps or lower based on either plan or participant assets. When utilized as



the QDIA, pricing can be 25 bps or lower, lessening the gap relative to TDFs, but not quite enough to overcome plan sponsor preference for lower-cost target date funds as the plan default.

This dynamic is beginning to change with improvements in recordkeeper data on both the plan (e.g., employer match and other sponsor benefits such as a profit sharing or defined benefit pension) and the participant that can be used to improve portfolio alignment with the needs of participants even without their engagement.

## The Future of DC: Personalized Investing

### Hybrid QDIA Solutions and Personalized TDFs

We believe the emerging ability to capture and integrate recordkeeper data at the individual participant level will power further improvements in portfolio personalization, both for managed accounts and TDFs alike. Plan recordkeepers have long captured more than just the age of participants, but also their gender, account value, salary, bonus, deferral, employer match and other plan sponsor benefits, all of which are starting to be fed to managed account services to provide improvements in personalization in the absence of any participant engagement. We believe this will, on the margin, further improve the argument for the use of managed accounts as a QDIA in that investment portfolios would be modified as needed based on differences not just in age but also individual retirement readiness relative to their age cohort when defaulted without any participant engagement.

This is especially true for Hybrid QDIA solutions, which typically feature TDFs as the initial default for younger investors and a transition to managed accounts based on investor age and potentially other factors as determined by the plan sponsor and recordkeeper. This design could provide strong merit if implemented and priced appropriately. Differences among younger plan participants tend to be small, supporting the use of TDFs initially, whereas differences among older participants become comparatively much larger over time, particularly as investors enter their 50s and approach retirement, potentially warranting managed accounts as a default when investment portfolios can be better personalized based on meaningful differences among older participants. In our view, the case to do so becomes even stronger the lower the fee of the managed account service.

As alluded to above, this same design can be utilized to better personalize TDFs as well, whereby a managed account chassis would use the same participant demographic information, namely income, savings rate, plan balance, etc., to enhance participant assignment and allocation to a TDF vintage portfolio(s) based on more than age alone. In this scenario, assignment would likely be enveloped by one portfolio more aggressive and one portfolio less aggressive than the baseline age-based portfolio and would likely involve the blending of two adjacent target date portfolios, e.g., a 2030 and 2025 portfolio to better achieve a desired investment portfolio and risk level.

### QDIA Model Portfolios

We expect the lines between TDFs and managed accounts may further blur, particularly with the rollout of QDIA model portfolios which leverage a managed account chassis to personalize model portfolios, not at the participant level but at the plan level. QDIA model portfolios, while very similar in form and function to custom target date funds (CTDFs), differ in that they are not “unitized”—there is no net asset value (NAV) struck at the portfolio level with participants owning units or shares of a fund. Instead, the managed account chassis is used to create custom portfolios made available not as “funds” but as “model portfolios” implemented as a series of funds at the individual participant account level.

QDIA model portfolios could be implemented as custom target date/age-based portfolios with plan sponsors offered the ability to select among pre-packaged glidepaths ranging from conservative through aggressive, whichever is best aligned with the plan demographics and sponsor preferences. And since there are no unitization or fund administrative costs, there’s no reason for portfolios to be spaced five years apart as TDFs are – instead, they could be designed for each individual age cohort. Moreover, they could easily integrate recordkeeper data to reflect differences among participants across income, savings rate, account values, etc., to personalize portfolios without any participant engagement as discussed above. Alternatively, QDIA model portfolios could also be implemented as custom target risk portfolios with investors aged into successively more conservative portfolios, creating a synthetic or stepped-glidepath. If paired with a risk tolerance questionnaire (RTQ), they could readily be provided with a risk overlay, ranging from a conservative to aggressive 50-year-old model portfolio, for example.



Importantly, QDIA model portfolios would likely be readily portable across all plans within a given recordkeeping system, making them vastly easier and less costly to implement than CTDFs, which remain principally a mega plan solution due to the complexity associated with constructing and managing custom glidepath portfolios and the associated cost of unitization services. Importantly, we expect QDIA model portfolios will not only be offered at no additional cost to the plan sponsor, but also likely include additional discounted fees for recordkeeping services, provided these solutions also incorporate the stable value and other proprietary offerings affiliated with the recordkeeper. So long as these solutions find a way to address the performance reporting requirements of plan sponsors and their consultants, we believe QDIA model portfolios may gain significant traction and uptake by retirement plans. This is likely to be especially true for small- to mid-sized plans long unable to access CTDFs, in that they overcome the longstanding objection to the use of managed accounts as a default, namely cost, while still providing material advantages in their ability to customize the asset allocation, vehicle type, asset classes and active/passive mix in a manner better aligned with plan demographics and sponsor preferences. Arguably, they will also be poised to better facilitate a hybrid QDIA solution, whereby participants would be seamlessly transitioned into a full-fledged managed account portfolio the moment they engage to volunteer additional datapoints related to their financial circumstances, goals and retirement intentions.

### **Advisor-Managed Accounts (AMA)**

Managed account and QDIA model portfolios are typically tethered to an embedded investment fiduciary initially responsible for the design and ongoing management of the solution, but that need no longer be the case. New business models are emerging whereby the investment fiduciary's role may be altered and/or altogether subsumed by an unrelated third-party consultant, investment advisor or plan sponsor willing to serve as the fiduciary with investment discretion for the managed account and/or QDIA model portfolios. This has long been the case for CTDFs, which are typically designed by a plan consultant and implemented on an advisory or discretionary basis on behalf of a large retirement plan. In the near future, we believe that the same will increasingly be true for both managed account and QDIA model portfolios across plans large and small, whereby both offerings will increasingly be designed or re-tooled to facilitate third-party advisor management.

AMA solutions may also permission the ability for advisors to impact a wide array of variables and assumptions that drive the way these solutions work, from the capital asset pricing model (CAPM) assumptions used for Monte Carlo simulations and corresponding estimates of retirement readiness to the asset allocation glidepath as well as portfolio allocations to foreign vs. domestic, large vs. small, growth vs. value, long vs. short duration, high vs. low credit quality, active vs. passive and so forth. Once these preferences are configured, they can be implemented across as few as one or potentially all plans managed by the advisor. AMA solutions could even be designed to use the same suite of non-plan investments to provide consistent portfolios across all of an advisor's clients in a manner unrelated to individual plan lineups.

Advisor management and control of participant data is uniquely positioned to provide not only a funnel of plan participants into managed accounts, but also into rollover IRA opportunities with the advisor. As this occurs, there is a unique opportunity to provide those same advisors a parallel experience to help them build and manage portfolios when they serve as Rep-As-PM for their wealth management clients. This is truly a massive opportunity, as broker/dealers (B/Ds) mobilize resources to amplify conversion of client accounts from commission-based to fee-based advisory relationships with annuity-like characteristics. Within advisory, while there has been significant acceptance and growth of third-party, discretionary model portfolio solutions, Rep-As-PM assets are roughly five times the size and are likely to remain several multiples larger than third party discretionary solutions. Accordingly, we believe B/Ds will need to better address Rep-As-PM risks and scale limitations through similar advisor-managed portfolio applications designed to guardrail activity, ensure asset allocation compliance, and move to model portfolios to create improvements in scale and profitability.

AMA is distinctly positioned to not only tailor investments to better meet plan sponsor needs and preferences, but also amplify the role and value of the advisor, who will increasingly provide advice not just at the plan but also participant level. In the special case of investment advisors affiliated with either a broker/dealer (B/D) or retirement plan aggregator (RPA), this provides the opportunity to democratize the availability of advice, with investment advisors providing participant advice far more broadly than before and in a manner more consistent with the advisor's wealth management practice and/or home office prescriptions. Increasingly, the investor will have the ability to talk with an investment advisor to answer their questions and access financial planning services – a boon for the investor and likely priced as a premium, add-on service.

This also has significant implications for IRA rollovers and wealth management considerations more broadly, with investors with smaller account balances remaining within the retirement plan where they can be better serviced via digital advisory services, and those investors with greater wealth and complexity rolling out of plan to receive enhanced financial, trust and

estate planning services. Irrespective of whether the participant remains in-plan or rolls out, we anticipate managed account services, especially AMA, will increasingly feature more comprehensive financial planning services, financial wellness offerings and advice with respect to insurance products, including whether to purchase life, disability, and especially longevity insurance. All of which provides a great segue to the final section and the arrival of annuities within DC plans.

### **Emergence and Incorporation of Lifetime Income Solutions**

With the recent passage of the Secure Act in 2022 and, notably, a safe harbor provision to plan sponsors who adopt annuities (which effectively immunizes them from future participant lawsuits), innovation in the decumulation and lifetime income space has been turbo-charged. The key enabler and beneficiary of these solutions will likely be TDFs, managed accounts, and especially plan participants themselves. With participants aging and approaching retirement, their focus is maturing from one of accumulation to decumulation, and the ability to adequately fund their lifestyle in retirement. Until now, plan sponsors, participants and consultants have all focused predominantly on how to save and invest enough to retire – but planning only to retirement rather than through retirement can cause participants to either spend too little and fail to fully enjoy their retirement savings or, alternatively, spend too much and ultimately be forced to dramatically curtail spending or altogether exhaust their savings in retirement.

We would posit that just as most everyone but for the most affluent should purchase life insurance to protect against premature death and its catastrophic impact on one's family and dependents, the same is true for annuities, with the vast majority of plan participants benefiting from the purchase of annuities to protect against the combination of uncooperative investment markets and long life. As our next white paper on Lifetime Income Strategies will cover in greater detail, self-annuitization is generally suboptimal, with most investors benefiting from the purchase of an annuity and its corresponding mortality credits to, in combination with Social Security, pension and other guaranteed income sources, fully fund essential living expenses in retirement.

That said, understanding the cost and complexity of the different annuity products and features, from Single Premium Income Annuities (SPIAs), Deferred Income Annuities (DIAs) and Qualified Longevity Annuity Contracts (QLACs) to Guaranteed Living Withdrawal Benefits (GLWBs) is daunting for plan sponsors and participants alike and explains the extremely low uptake within DC thus far despite the strong benefits that accrue to investors. It's for this reason that we believe uptake will only happen if facilitated through professionally managed portfolio solutions, namely TDFs and managed accounts. Here, tremendous innovation is already underway. A handful of TDF solutions have already been launched in recent years which incorporate the purchase of SPIAs, DIAs, QLACs or GLWBs and similar innovations are beginning to play out across managed account providers. The benefit of this approach is manifold, from the use of third-party financial experts overseeing the selection, negotiation and monitoring of the specific annuity product and insurance provider, determining how much to annuitize and how to modify corresponding portfolio allocations, as well as leveraging the pooling of participant assets to do so on more advantageous terms – particularly without commissions of 5% or higher – than available to individual investors in the retail market.

Since the decision to annuitize and how much to do so is deeply individualized, most TDFs are likely to do so via a binary approach whereby the participant is presented with the option as early as their 50s or as late as the date of retirement to either remain in the non-annuity version or alternatively branch off into the TDF version with a pre-established purchase of annuities. In contrast, managed accounts will likely offer significantly greater flexibility and personalization, including advice on not just whether to annuitize, but also how much to annuitize, which annuity products to use, and how to adjust the residual investment portfolio appropriately.

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