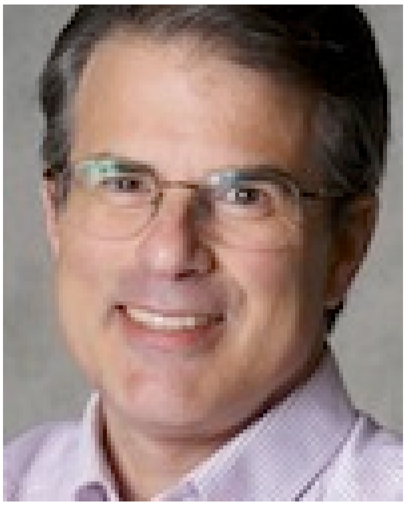
At DCIIA Forum, Familiar Faces and Fresh Ideas

By Kerry Pechter *Thu, Dec 1, 2016*

Does automatic enrollment lead to higher consumer debt? Should employers stop sponsoring retirement plans? These are other ideas were floated at the Defined Contribution Institutional Investors Association Academic Forum in New York yesterday.



Where, in one place and at one time, can you meet about 350 of the people, including asset managers, recordkeepers, actuaries, academics, consultants and entrepreneurs, who help determine what the rest of us think about when we think about the defined contribution business in the US?

Gathered in the Goldman Sachs building in lower Manhattan yesterday for the Defined Contribution Institutional Investors Association's seventh annual Academic Forum, I saw people who have, almost like the tugboat captains who used to nudge ocean liners around the adjacent New York harbor, spent years nudging millions of people and massive blocks of assets toward solvent retirements.

Dropping the women's names first, there was Kelly Hueler, creator of Income Solutions, Stacy Schaus of PIMCO, Lori Lucas of Callan Associates, Toni Griffin of MetLife, former MetLife retirement chief Jody Strakosch, Melissa Kahn of SSgA, and Cindy Hounsell of WISER.

Among the men, there was Brett Hammond (formerly TIAA), behavioral economists Meir Statman and John Beshears, EBRI data wrangler Jack Vanderhei, Franklin Templeton's Drew Carrington, and Richard Fullmer of T. Rowe Price, Josh Dietch of Strategic Insight and lawyers Jonathan Forman of the University of Oklahoma and Michael Kreps of the Groom Law Group.

As noted above, hundreds of other retirement professionals attended. Over the past half-decade, under the executive direction of Lew Minsky, DCIIA's membership has quietly grown to include almost the entire roster of financial institutions that run the trillions of dollars in tax-deferred retirement savings. Every fall, the organization holds an academic forum where scholarly research is presented and discussed.

Yesterday, in an auditorium that Goldman Sachs' own CIA-trained security expert said is the safest space in the safest building in Manhattan, the presentations did not address topical issues like 401(k) litigation or the new DOL fiduciary rule but instead some of the more perennial or fundamental issues that the retirement industry faces. Such as:

'Auto-Enrollment: Comprehensive Plan Design'

In perhaps the most provocative presentation of the day, Harvard economist John Beshears questioned the efficacy of automatic enrollment (AE). Although AE has indisputably raised participation rates of 401(k) plans, many participants have nullified their savings by taking on more consumer debt, his research showed.

Looking at payroll and credit rating agency data on civilian employees of the U.S. Army, Beshears and his co-authors found that about 60% of their savings in the government DC plan, the Thrift Savings Plan, was offset by new debt. Moreover, if the government's matching contribution were excluded, virtually all of the employee contribution was offset by new debt, on average.

Jack Vanderhei of EBRI, whose voluminous output of data usually shows the 401(k) system to its best advantage, did not dispute the findings. But he said that EBRI's projections suggest that when a company moves from voluntary enrollment to AE with automatic escalation of contribution percentages, participants end up with at least a 17.5% increase in "simulated retirement outcomes."

'Shark Attacks and Our Work: How Our Beliefs & Abilities Enable Us to Retire'

Two academic economists, Raphael Schoenle of Brandeis University and Geoffrey Sanzenbacher of Boston College, consider two questions, respectively. The first was, "Why don't young people save more and why don't retirees spend more?" The second was, "Which jobs can older minds and bodies do best (and worst)?"

Younger people tend to underestimate their lifespans (and fail to save adequately for retirement) and older people on average overestimate their lifespans (and hoard against the possibility of needing long-term care), Schoenle said in answer to the first question. The crossover age, when people on average know how long they are likely to live, is about 73. Plan participants need more "probability literacy," he said.

Sanzenbacher introduced a "Susceptibility Index," a scale covering 52 separate physical, cognitive and sensory abilities and 900 different occupations that enables him and his co-researchers to identify the jobs that older people can or can't handle as well as younger people. “Blue collar” work, not surprisingly, tends to get much harder for people in their 60s—an observation that may dissuade policymakers from raising Social Security’s full retirement age.

‘Long-Term Investing in a Short-Term World’

In a discussion aimed at the asset managers in the room, Meir Statman of Santa Clara University took on the question of whether funds that follow ESG (Environmental, Social and Governance) and SRI (Sustainable and Responsible Investment) guidelines belong in 401(k) plans and Russell Wermers of the University of Maryland addressed questions regarding the place for actively-managed funds in 401(k) plans.

Because ESG/SRI funds invest in companies based on ethics as well as profitability, and because actively-managed funds tend to take bigger risks and charge higher fees (relative to index funds), both test the fiduciary responsibility of plan sponsors to help participants maximize the growth of their savings in a prudent way.

Wermers’ research showed that active funds that are managed with a long-term focus (but not simply buy-and-hold) can outperform high-turnover funds by as much as 3% a year over a five-year period, thus justifying their higher fees. Statman, for his part, claimed that the pleasure that many investors get from owning ESG or SRI funds is a fair substitute for the fund’s under-performance, if any. “People care about more than money,” he said.

‘Four Decades Since ERISA: Rethinking How We Allocate Risks’

Should employers, who have largely abandoned the defined benefit pension business, also get out of the defined contribution business? Dana Muir of the University of Michigan said employers shouldn’t bear the fiduciary risks and administrative costs of plan sponsorship and pointed to experiments in Canada and Australia with non-employer plans.

Going a step farther, Jonathan Forman suggested taking insurance companies out of the retirement business by creating “tontines” instead. Like a traditional annuity, a tontine consists of the pooled investments and longevity risks of a large group of people.

Unlike a traditional fixed annuity, a tontine doesn’t involve guaranteed payouts; participants accept market returns and rely on mortality credits for most of their yield. Annuities in general might be more popular, he said, if the government taxed annuity income at a rate lower than the tax on ordinary income.