‘Smart,’ from UK, Enters the US PEP Market

By Kerry Pechter *Fri, Jan 14, 2022*

'Smart' is the recently-launched American branch of a British fintech with expertise in a kind of retirement savings plan that's called a 'master trust' in the UK and a 'pooled employer plan' or PEP in the US. RIJ interviewed two of its top executives.

During a Zoom conference last fall on the future of defined contribution (DC) plans, I used the “Chat” function to chat up another attendee. Sidebar conversations during webinars are wrong, apparently—like passing notes in class. I might have lost my seat at the conference because of it.

But I wanted to make contact with that other attendee, Catherine Reilly. She’s the director of Retirement Solutions at **Smart**, the recently established US branch of a substantial defined contribution retirement plan recordkeeper in Britain called **Smart Pension**.

In the UK, Smart runs a $2.7 billion, 80,000-employer “master trust.” That’s the British version of Pooled Employer Plans (PEP), the multiple-employer plan design enabled by the SECURE Act of 2019. In the US since October 2020, Smart’s “recordkeeping solutions and retirement income solutions are purpose-built for PEPs,” according to its website.

With US headquarters in Nashville, Smart is moving fast. With capital from JP Morgan, Barclays, Natixis, Chrysalis, and Legal & General Group plc, Smart has just bought **Stadion Money Management**, a managed account provider, and is partnering with **Finhabits**, a provider of bilingual (Spanish/English), smartphone-mediated financial services.

For *RIJ,* Smart is interesting because it aims to reduce the often clunky process of accessing 401(k) savings in retirement to a few thumb strokes on a smartphone or key strokes on a laptop, while also helping retirees bucket their savings into short-term, medium-term and long-term money.

Historically, US recordkeepers have performed this critical function reluctantly, inefficiently or not at all. But without it, they’re just giving retired participants a reason to roll their money over to an (expensive) brokerage IRA. “The retirement income feature keeps people in the plan,” Smart’s US CEO Jodan Ledford told *RIJ* in an interview. “This optimizes their ability to preserve their base.”

The ‘grout in the mosaic’

Jodan Ledford, CEO of Smart USA

Ledford is responsible for growing Smart in the US. He already has a track record here. In his last job, he grew Legal & General’s US asset management business seven-fold, to $210 billion. Despite his British-sounding name, he’s an American. He tends to describe Smart’s services in metaphors.

“I like to use the term, *mosaic*,” he said in the interview. “In a pooled employer plan, for instance, the investment manager, the recordkeeper, and the plan administrator would be the pieces of the mosaic, and we could be the ‘grout.’ Or we could be the pooled plan provider that selects the other pieces.

“We will likely partner with recordkeepers to offer PEPs. Or we could be the 3(16) TPA (the third-party administrator, with fiduciary responsibilities). What we don’t provide is the 3(38) role (the asset manager with fiduciary responsibility for managing the investments in the plan).

“Say, for instance, that we approach a large registered investment advisor (RIA) or broker-dealer with financial advisers who serve small business plans. We say, ‘You can be the 3(38) fiduciary and select the funds.’ The RIA tells its advisers, ‘Here’s a new pooled employer plan. We have a system that lets you sign up the small business clients in less than hour.’ It lets the RIA or the broker-dealer do more business with small plans,” Ledford said.

“We could also partner with a recordkeeper, or with a large pension risk transfer company,” he added. "They could say to their corporate client, 'If you liked our annuity for your defined benefit plan, why not use this retirement income system for your defined contribution plan?'"

Smart sees existing asset managers and recordkeepers held back by older technology systems that hinder them from providing what people now take for granted: fast, easy onboarding of new clients; personalized solutions; and scheduling of customized money transfers from any plan account to any bank.

The SECURE Act made it legally easier to aggregate many small plans into a single large plan (a PEP) that a large asset manager or recordkeeper could, in theory, administer for much lower expenses than individual small firms currently pay. But those large service providers don't necessarily have the integration tools (e.g., the **Application Programming Interface** or API software) necessary to fill in the communication gaps between lots of unrelated clients and partners—like participants' banks. Smart (and its competitors) aim to furnish some of those tools.

No annuity feature—yet

These tools will allow Smart to help retirees take systematic withdrawals from their 401(k) plans. Reilly, the Smart executive in charge of Retirement Solutions, told *RIJ* that Smart's "decumulation platform" will give retirees "the flexible access of an IRA" while their money stays in the 401(k) plan.

Catherine Reilly, director of
Retirement Solutions, Smart USA

"It's a guided journey into retirement," said Reilly, whose varied career has included stints as a McKinsey consultant in Helsinki, overseeing State Street Global Advisors' $70 billion target date fund suite, and senior fellow at the Defined Contribution Institutional Investment Association. "You can set up a paycheck or move money around. It might be most closely related to a managed account." [Under US labor law, managed accounts, along with target date funds, are Qualified Default Investment Alternatives into which the payroll deferrals of new, auto-enrolled participants can be automatically deposited.]

Smart uses a time-segmentation or bucketing approach, dividing income distribution into four periods:

- A flexible spending account providing systematic withdrawals between age 65 and age 80
- A rainy day fund for emergencies at any age
- A "later-in-life" reserve fund for spending after age 80
- A legacy fund, if needed, to provide bequests to children, charities, etc.

The current product doesn't incorporate the option to purchase an annuity, but it may eventually allow for the purchase of a deferred income annuity (DIA) for guaranteed income in old age. Legal & General sells immediate annuities in the UK, but according to Reilly, won't be marketing annuities through Smart. Instead, the Smart platform calculates a "sustainable income" for every year of retirement up to age 80.

"Monthly payments can be set up, and you can always change them or make flexible withdrawals," Reilly said. The system suggests an asset allocation, but the payments, once set, won't automatically adjust or rebalance in response to market volatility.

"In the US, the recordkeeping industry has struggled to issue paychecks. Sometimes the recordkeeper is the problem. Sometimes plans just weren't designed for retirement income payments," Ledford told *RIJ*.

Replicating UK success

How does Smart get paid? "If we provide recordkeeping services, it can be basis points, flat dollar, or mix of both. Flat dollar is popular now," Ledford said. "In the PEP-only model, we'd charge basis points. Either way, we're trying to provide the service at a cost point that's not a barrier to entry. In the small market today, according to the benchmarking we see, a small plan pays about 260 basis points (2.6%) a year in fees. We want the cost to be under 100 bps (1.0%) all-in."

In the US, Smart hopes to repeat its successes serving retirement plans in the UK, Ireland, and Dubai. In the UK, it's a major provider of a defined contribution "master trust"—the UK equivalent of a pooled employer plan in the US—serving more than 80,000 employers in Britain and 900,000 participants whose plans have £2 billion ($2.74 billion) under management.

Smart's recent acquisition of **Stadion** adds a ready-made chunk of US business. Stadion provides personalized managed account services to some 4,000 retirement plans with $2.3 billion in the US. Stadion serves as the fiduciary that chooses the funds and designs the glide paths for the managed accounts.

Smart's partnership with **Finhabits** will give it access to the Latinx community in the US, where there are an estimated 4.65 million Hispanic-owned small businesses, many of them lacking retirement savings plans.

What obstacles might Smart face in the US? So far, it seems to bill itself as a retirement jack-of-all-trades, refusing "no job, big or small." That's a key that could unlock a lot of doors. One potential speed bump: Prospective clients in the US might wonder if they have to hire at least some of Smart's partners—like JP Morgan, Stadion and Legal & General—in a bundled solution. But Reilly said, "By buying Smart you're not committing to any of our partners."

Another possible hitch: Smart could be misgauging the way retired Americans tend to use their 401(k) money. In fact, many of them tend *not* to start taking money out of their retirement plans until the government forces them to at age 72. Distributions are taxable, and so not to be taken lightly. Investment advisers often tell clients to spend tax-deferred money last.

In the managed account market, it will certainly face competition from providers like Morningstar and Edelman Financial Engines. But the managed account market is big. According to **Cerulli Associates**, "The top nine DC managed account providers comprised more than $400 billon in DC assets and the vast majority of DC recordkeepers now partner with at least one managed account provider." Smart may end-run that traffic by specializing in helping big asset managers and recordkeepers address the burgeoning PEP market—the kind of market Smart appears to have mastered in the UK.