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The ‘PEP’ era begins

By Editorial Staff *Wed, Jan 6, 2021*

Only 26% of 401(k) plan sponsors say they are at least “somewhat interested” in joining a pooled employer plan (PEP), according to new report from Cerulli Associates.

The “PEP” rally is starting slowly. But we’re only a week into it.

As of January 1, 2021, unrelated employers—not bound by a common industry, trade union or even geographical locality— can join a single 401(k) plan, called a pooled employer plan (PEP). The bipartisan SECURE Act of 2019 amended labor law to make PEPs possible.

But only 26% of 401(k) plan sponsors say they are at least “somewhat interested” in joining a PEP, according to Cerulli’s new report, *US Retirement Markets 2020: Exploring Opportunities in the Small Plan Market.* Among sponsors of existing “micro” plans with under $5 million in assets, just over one-third (36%) had “no opinion” on the topic.

“This may be the sign of a knowledge gap related to PEPs in the lower end of the market,” said Shawn O’Brien, a Cerulli senior analyst, in a release. “When addressing smaller employers, more educational discussions related to the costs and benefits of PEPs may be in order.”

Recordkeepers, advisors, and asset managers also exhibit varying levels of interest in either sponsoring or joining a PEP. Some have already announced plans to launch a PEP in 2021. Others are taking a “wait and see” approach to PEP opportunities. About four in 10 (39%) would “consider participating in the PEP market if approached by an advisor or consultant.”

So far, Aon, Mercer and Principal Financial have announced their intent to act either as PPPs or as service providers within PEPs. But they are outliers. Fewer than one in five (17%) defined contribution (DC) recordkeepers say they are looking to become service providers within a PEP or intend to act as the umbrella or general contractor of a PEP by becoming a pooled plan provider (PPP).

Of the plan advisers who intend to sell PEPs to employers, the majority will target “micro” and “small” plans with $25 million or less in plan assets, as well as employers without an existing workplace retirement plan. For employers with no plan, PEPs will be “sold, not bought,” Cerulli believes.

It remains to be seen what proportion of companies joining PEPs will switch from an existing plan—and bring a pool of assets and participants with them to the PEP—and what proportion will not have previously had a plan.

To help close the retirement plan "coverage gap"—only about half of US full-time employees have access to a tax-favored workplace savings plan at any given time—PEPs will have to attract the latter type of company.

What's in it for the employers? PEPs can relieve them from many of the administrative burdens associated with offering a standalone retirement plan, and reduce their costs by enabling them to purchase retirement plan services with greater economies of scale.

"Small businesses often lack the benefits personnel and investment committees often housed within larger organizations," O'Brien said. "Smaller plan sponsor clients aren't necessarily looking for a best-of-breed custom target-date fund or a robust financial wellness program. Rather, they want a provider that can support them through the administrative challenges of offering a retirement plan."

For providers, PEPs could be a vehicle for capturing more clients in the small plan market. For big asset managers, PEPs can aggregate many small pools of assets at small plans into pools of assets large enough to serve economically.

As recordkeepers, asset managers, third-party administrators (TPAs), and intermediaries navigate PEP opportunities, configuring an effective service model will be crucial. Cerulli suggests the flexibility around the type of individual or entity that may serve as a PPP, along with the range of fiduciary responsibilities involved in operating a PEP, could lead to a variety of models. "Providers considering the role of PPP need to be aware of the 3(16) fiduciary responsibilities involved," said O'Brien. "Recordkeepers and TPAs are seemingly a natural fit for this role."

PEPs aside, other providers have launched bundled solutions geared toward smaller plans to broaden their market presence and create new product distribution opportunities. Providers seeking to gain adoption in the small plan market must contend with the unique demands and constraints of small business employers and grasp the competitive differentiators specific to this market segment. Developing a simple, cost-conscious, easy-to-onboard 401(k) solution is merely the first step to succeeding in the small plan market, Cerulli said. Providers will also need to guide plan sponsors through some of the challenges associated with administering a retirement plan.