Collective Retirement Savings Arrangements: A Future for Retirement Savings?

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Current Environment

- The end of the pure DB plan
- Aging population/demographics
- Need for Financial Wellness education/tools
- Retirement Savings Gap
- Governance and Administration
- Fee Issues
The End of the Pure DB Plan

• Providing the promised benefit is difficult
  – Investment and longevity risk
  – Increase in deferred and retiree populations
• Many plans now closed to new EEs if not closed to all
• Most implement DC type plans for future accruals
• Expectation is few or none will exist within 10 years
The End of the Pure DB Plan

- In the UK. There are about 32,000 small schemes (including DC schemes) covering about 200,000 active employees
- On the DB front about 90% of the plans are closed, at least to new EEs and have more retirees than actives
- Funding requirements of closed plans are very expensive and annuity costs significantly greater than Canada or U.S.
The End of the Pure DB Plan

- In the U.S., a similar story, closing of DB plans to new employees, offering lump sum buy outs and purchasing annuities (buy in or buy out) to reduce risk
- In Canada, again a similar story.
  - Funding obligations are lower than in the UK but greater than in the U.S. as are the costs to purchase annuities
  - There are only about 1.2 million EEs in registered pension plans (DB and DC)
Aging Population/Demographics

- In Canada, about 90% of Employers have less than 100 employees
- Not likely much difference in UK, U.S. and other countries
- Retirement savings plans for employees have a significant cost in terms of fiduciary and administrative duties and many individuals with entitlements have left the organization
Aging Population/Demographics

- ERs no longer want or can manage the risks tied to DB pensions
- While decumulation issues for individuals are known, is there a similar concern for our investment managers and consultants
- In DC type plans, with many older long service EEs leaving, the ongoing contributions are not sufficient and the investments have to be sold.
- Consider programs such as the Canada Pension Plan and the U.S. Social Security programs. What occurs when distributions exceed contributions?
Financial Wellness Education/Tools

- While a great benefit to the Employer to have employees in control of their on-going financial and retirement needs, can we truly expect most ERs to have the ability or desire to address this?
- Providers are building tools to address the need, often very basic. In many cases, the usual end is referral to a financial planner/consultant who comes with a cost.
- On the DC side or in other vehicles such as RRSPs, IRAs and such other accounts in other countries, the individual is on her/his own.
- Pension scams exist in many jurisdictions, most notably recorded in the UK where a recent scam has netted about 55 million pounds. The question of whether the advisor is working for the individual or themselves is a significant issue.
- Fees tied to funds/ for financial planners on small or individual accounts are significantly higher than or larger plans which has an impact on the longer term ability to finance one’s retirement.
Governance and Administration

- A growing issue with some difficult issues to address again especially for the small employer.
- Is the fund manager/financial planner investing in the best interest of the individuals or in the interest of the fund manager?
- Has one compared the returns and options available to the members?
- Has one reviewed their communications to ensure that it is not making promises that may not be achieved?
Governance and Administration

- In the U.S., court challenges have grown against the plan sponsor
  - In one case, the challenge is with respect to a DB plan in a surplus position
- In the UK, a history of assets not being “prudently” invested in the interest of the members and scams where individuals lost significant retirement assets, leads to a great deal of pressure on sponsors
- Finding and tracking ex-employees, retirees, ex-spouses, adds a significant amount of work as the plans mature in all jurisdictions
Fees

• In the U.S., large 401(k) plans have fees around 0.47% of assets, for small plans, it is around 1% higher than this

• In Canadian programs, we see fees average about twice this level or above

• Individual fees for those without an employer sponsored plan or at termination/retirement when they leave the plan will likely be much higher
Fees

- With respect to fees, studies and many ads we now see identify the impact of a 1% fee during the accumulation period as reducing the retirements savings by 30%.
- Warren Buffet did a calculation for a 77 year period, his time in the market when he did the calc.
  - He invested money in the stock market and left it there, obviously it would have grown significantly. He then applied a 1% annual fee each year over the 77 years.
  - The impact of the 1% fee reduced the assets by roughly 50%.
- In Canadian money purchase programs, we see fees average about twice this level or above.
- Individual fees when they leave their ER program at termination or retirement may/likely are higher.
- ER sponsored programs have a longer time frame than an individuals accumulation period.
The Future? for Retirement Savings

- Collective Retirement Savings Programs
- The UK, NEST and Master Trusts
- The U.S., OregonSaves, legislative changes toward Multi-ER rules, etc.
- Canada, Jointly Sponsored Programs, etc.
Collective Retirement Savings Programs

- These have existed for many years and what now being introduced has been considered for many years.
- Legislation generally limited such programs to ERs who were linked, Multi-ER union or association plans (MEPS) or Jointly Sponsored Plans (JSPP).
- It should be noted that these plans were not without problems for reasons similar to single ER plans.
  - An example, in one U.S. program for auto suppliers was impacted by the recession and new technologies, many went out of business, bankrupt or had significant shutdown periods, plan deficits grew as the investments shrunk and there were far fewer ER's and members
  - Some plans and their Trustees made investment choices that were more in the interest of the Trustees than in the interest of the Members
  - In Australia, currently there are issues with a number of the Funds for similar investment related reasons
- There are some Ontario JSPPs that have done very well and are growing the Collectives Model. One grandparented program in Saskatchewan may show how best it can be done.
Collective Retirement Savings Programs

- The newer push towards these programs may be to address the Retirement Savings Gap for those who do not have an ER sponsored retirement program.
- In the UK, the first step was NEST, a mandatory program for all ERs who did not provide a retirement savings program for their EEs.
- In Canada, it was the PRPP, however, each jurisdiction had the option to establish as a mandatory or optional program. All except for Quebec chose optional.
- In the U.S., about 40 states have looked at with Oregon being the first “off the block”, others are following.
- Following this start, other opportunities have arisen.
**Collective Retirement Savings Programs**

- In the UK NEST legislation was introduced more than 10 years ago with a phase-in plan which was delayed until 2014.
- There is no cost or Fiduciary responsibility for the ER. Their role is limited to dealing with new EEs, re-enrolments (every 3 years) and terminations.
- There are roughly 7.9 Million members and about 5.7 Billion in assets, annual fees are .3% with an initial charge of 1.8% of contributions.
- At retirement, money can be left in the program and several options exist to drawdown your money in retirement or such can be transferred.
Collective Retirement Savings Programs

- In the UK, the legislation is/has pushed the concept of Master Trusts and due to Governance/admin issues that has arisen, there is a new somewhat cumbersome and aggressive compliance requirements.

- On the DC side, there were initially around 80 funds apply for Master Trust status with final documents to be filed by April this year, more than 40 have dropped out of the running, merging their assets with others, of the 38 or so remaining, only 10 have been approved to date and a few were give extensions to file the necessary documents.

- Within the Master Trust space, there are about 14 Million members at this time.

- Where an ER participates in a Master Trust, most fiduciary responsibilities end, costs to the ER are reduced as are fees charges against the assets.

- There is no cost or Fiduciary responsibility for the ER. Their role is limited to dealing with new EE’s, re-enrolments and terminations.

- The Regulator’s goal is to eliminate all ER sponsored schemes.
Collective Retirement Savings Programs

- In the UK, on the DB side, there are a small number of Master Trusts but final rules and regulations are not fully in place. As of August 1, deferred to next year.
- On the DB side, there are about 5000 DB schemes (most closed to new EEs) with 10.5 million participants and about 4.5 Trillion in assets.
- Concerns arise tied to the strength of the ER’s “covenant” and how each plan moves into the Master Trust and to protect all within the scheme.
- For a Plan Sponsor, moving into such will reduce fiduciary and admin responsibilities, reduce the funding costs and provide better security for EEs and retirees.
- Buying annuities in the UK to get these liabilities off the books is very expensive, annuity purchases require the use of the Gilt rate, a closed plan may have a valuation rate around 2% while the Master Trust may be able to support a 4% or higher rate.
- One prospective Master Trust expected to start up with about $10 Million in seed money and expected to grow quickly to about 600 Billion in assets.
Collective Retirement Savings Programs

• In the U.S., over the past few years, there has been talk/initiatives to require ERs with no Retirement savings program to enroll employees in a mandatory IRA program or in a state run program.

• In a large program costs would be reduced to the member, as a collective program, the ER would have little admin and fiduciary responsibilities and the EE’s would see lower fees and better for financial education.

• The first program with a successful start up is OregonSaves, a couple of programs such as in Seattle/Washington did not get out of the starting gate.

• After 2 years, it has around 81,000 members though about 5950 ERs and assets of about $11 million, the phase end period for smaller ER’s is as of July 2020.

• CalSaves follows the start up in Illinois effective for July 1 with a phase in period for smaller employers who must sign up by 2022.

• Recently, Oregon is looking at allowing participants from other states such as those interested from Seattle or other states who might wish to avoid some of the start up issues and become part of a larger program immediately.
Collective Retirement Savings Programs

- In the U.S., there is a growing interest in allowing decumulation options from within the 401(k) and other DC plans. Individuals would remain in familiar program, likely with lower fees and would result in the allowing the 401(k)/DC programs to maintain their size or grow.

- As of August 1, legislation effective September 30, will permit employers to connect with associations of employers in a city, county, state, or a multi-state metropolitan area, or in a particular industry nationwide to provide retirement plans for their employees.

- This would be attractive to smaller employers who would benefit from less fiduciary and administrative duties and EEs would benefit from the lower fees charged to a large plan.

- Further discussions are also considering whether one might allow Banks and Insurance companies to establish Collective Retirement savings programs, similar to UK Master Trusts or Australian Superannuation Funds.

- In the U.S., there is also some interesting situations with respect to public sector/quasi public sector plans. In some states plans are being merged to accomplish savings and better governance and improve funding. In other states, this has been determined to not be in the best interest of the state finances.
Collective Retirement Savings Programs

- In Canada, the PRPP was in its background a program similar to Oregon Saves, Nest. It would be as a minimum a program which would require all employers without a retirement savings program to participate in a PRPP. It would have limits on the fees which could be charged and would be set up by Insurers/Banks others who would operate the program.
- However as mentioned earlier, the issue on mandatory participation was left up the various jurisdictions across Canada and only Quebec opted to implement the mandatory requirement.
- While this was heralded as a great idea whose time has come, much like Seattle, there has been no take up in any jurisdiction even in Quebec even though this would be attractive to smaller employers who would benefit from less fiduciary and administrative duties and EEs would benefit from the lower fees charged to a large plan.
- Smaller ERs did not like the costs or duties required to set up, register and maintain a DC pension plan. The alternative was a group RRSP, required on an enrolment and sending money. ER contributions would attract payroll taxes (CPP,EI,WCB and EHT) but if they wished to make contributions they could set up a separate DPSP avoiding the payroll taxes.
- The number of these types of programs more than doubled in the past 5 or so years.
Collective Retirement Savings Programs

• As one cannot find a PRPP in Canada, the Group RRSP/DPSP alternative has grown at little cost to the ER but likely much higher fees to the EE that would have been available under the PRPP.

• As in the U.S. and elsewhere, there is a growing interest in allowing decumulation options from within DC pension plans. Individuals would remain in familiar program, likely with lower fees and would result in the allowing the DC programs to maintain their size or grow.

• One existing example will be reviewed later.
Collective Retirement Savings Programs

- On the DB side, a variety of Public Sector/quasi public sector plans became Jointly Sponsored Pension Plans and rules within these programs differ from pure DB plans with often the member at risk with respect to future indexing of their retirement benefits.
- These plans are not subject to the same funding rules as pure DB plans and in Ontario are not subject to Guarantee Fund fees/protections.
- In Ontario, programs such as the Ontario Public Sector Plan (OPTrust), the Hospitals of Ontario Plan (HOOPP), the Teachers Pension Plan, Ontario Municipalities (OMERS) and Community Colleges Plan (CAAT) are some of the largest pension plans in Canada.
- Legislation was enacted that allowed these plans to add non-associated Employers into their programs. As a result there has been a growth in existing single ER DB plans joining these programs.
- Three universities in Ontario have also moved in the direction and expect other Universities may join in later. The benefits being a larger size, spreading risk, a separate board administration centralizing administration and fiduciary responsibility.
- A couple of other private sector groups are attempting to establish similar collective plans.
Collective Retirement Savings Programs

- To accomplish such a merger, the plan must communicate to all current members, all members with deferred pensions and all pensioners and hold a vote.
- If the vote is successful, the plan being transferred must satisfy the exiting plans requirements and going forward accruals are the same for all. Benefits and pensions in pay remain as defined in the plan up to the date of transfer.
- If we look at a Transfer of TorStar into CAAT, all benefit accrued or in pay would be fully guaranteed under the CAAT program. The assets transferred to CAAT from TorStar were sufficient to full fund those liabilities and the surplus level in the CAAT plan.
- Going forward, EE and ER contributions and benefit accruals would be the same. While CAAT provides indexing, such indexing provisions would not apply to the pension or benefits accrued prior to their joining CAAT.
- In the Universities merger, the 3 have agreed to a funding formula which requires the unfunded liabilities from the existing plans to be funded over the next 10 years, EE and ER contributions and benefits will be the same for all going forward.
- OPTrust is bringing in smaller quasi-public sector ER’s into its program.
Collective Retirement Savings Programs

- In other Canadian situations, the move is towards Target Benefit Plans, essentially similar to Multi-ER in that a fixed contribution would be made by EE and ER and the benefits could be adjusted depending on the funded status of the plan. This along with the merger of many Public Sector programs in New Brunswick has improved the funded status of the programs.
- Prior to 1978, legislation allowed DC plans to have decumulation options, one plan that was grandparented was the CSS Pension plan that stared up in 1939 in Saskatchewan.
- Represents more that 330 employers in 8 provinces with 48,000 participants and roughly $4.6 Billion in Assets
- Members on retirement can leave the money there or transfer out if they wish. Options exist to elect a fixed pension benefit within the plan, to decumulate which would vary based on their investment performance in the plan, or any combination of the above.
- Fees under the plan are roughly .57% and this includes access to Financial Consultants who assist in the individuals planning and available choices at no cost. These fees are close to 2% lower than what most charge.
- This seems like the type of plan we all want to be in or allow.
Key Takeaways

- Major changes are coming to the Retirement savings industry
- If these programs do benefit the participants, why are not more ERs/EEs demanding them
- This will be a great disrupter for the Financial Services/Consulting Business
- Do I wait for this to happen or do I jump in ASAP