Issue Brief

Retirement Policy: Potential for Changing Roles of Employers in Retirement Programs

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Key Points

- Approximately one-third of all private-industry workers in the U.S. lack access to an employer-sponsored retirement plan. These workers are often employed at organizations that are small and lack the financial and human capital resources to sponsor a retirement program.
- Shifting retirement plan responsibilities and related liability to a third-party entity and away from the employer—"decoupling"—may be advantageous to both employers and employees. Employers may see reduced costs, risks, and administrative burdens, while employees may benefit from additional options and retirement income solutions.
- Decoupled retirement plans have been introduced in countries outside of the U.S., and they are becoming more prevalent in the U.S. through structures such as state and local government-based retirement initiatives and pooled employer plans under the SECURE Act. While some employers will likely retain their own single-employer plans, the trend toward decoupling will likely continue.

Introduction

In July 2019, the American Academy of Actuaries published an issue brief titled *National Retirement Policy & Principles*. The brief focused on the increasing need for the establishment of a comprehensive national retirement policy based on certain guiding principles. In April 2020, the Academy followed up this issue brief with another titled *Retirement Security Challenges: Portability and Retirement Income*. That issue brief addressed the challenges faced by workers in a mobile workforce who accumulate retirement benefits at multiple employers over their careers. The issue brief focused on two specific risks faced by those workers: the potential for them to lose track of benefits and the challenge of converting accumulations/benefits into sustainable retirement income. Building on these efforts, a second follow-up issue brief titled *New Retirement Plan Designs: Degrees of Risk Sharing* was recently released; it identifies newer employer retirement plan designs that highlight methods of risk sharing and that have been used by some plan sponsors.

Driven by the ever-changing and -evolving relationships between employers and workers/employees, this issue brief explores redefining the role of employers involved in retirement programs by removing from employers many of the direct responsibilities for retirement plans. Under this approach, employers would not need to take on the full fiduciary or other responsibilities for a retirement plan; at least some of these responsibilities could be shifted to and fall on third-party entities (TPEs). These entities

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could be subject to government oversight as well as ERISA[1] regulations and guidelines. An employer's responsibilities could thus potentially be limited to the due diligence necessary for the selection of the TPE[2] and any transmission of employer and employee contributions to the TPE. Of course, employers could still choose the current approach and the associated responsibilities. In this issue brief, the approach of reducing employer involvement and responsibility is called "decoupling," and retirement programs that utilize some degree of decoupling are called "decoupled plans." A range of decoupling solutions could be available depending on the needs and goals of employers and employees.

Current Environment

A substantial percentage of employees (especially those working for smaller employers or as "gig" workers) are not covered by employer plans.[3] Some who are covered by employer plans may not be well-served by the specific offerings of those plans (for example, in defined contribution programs, there may be limited investment choices or high fee levels). Employers might avoid incorporating certain plan options (for example, in-plan annuities) because of the potential for additional fiduciary liability. A mobile workforce, where an individual could have many jobs during his or her working career, can have limited (or potentially no) retirement coverage or end up with a patchwork of retirement benefits from multiple employers.

Decoupling plans from employers has the potential to increase coverage,[4] better meet individuals' needs, provide for greater efficiency in the retirement benefit accumulation process, and offer distribution options or other features that employers on their own cannot offer or may choose not to offer. On the other hand, if an employer chooses to have only limited ongoing involvement with the program (e.g., leaving all employee

1 *Employee Retirement Income Security Act of 1974.*
2 In the case of the state and local government-based retirement initiatives discussed later in this issue brief, due diligence is not currently required of the employer; these programs may be required to be offered by employers that do not offer another employer-based plan.
3 According to the Department of Labor, in 2020 only 53% of private-industry workers at businesses with fewer than 100 employees, and 67% of all private-industry workers, had access to a workplace retirement plan (Bureau of Labor Statistics; *National Compensation Survey: Employee Benefits in the United States*; Table 2; March 2020.)
4 State and local government-based plans as discussed below have already achieved this to a certain extent.

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communications to the provider), decoupled plans can run the risk of employee confusion about the employer's role, employer and employee responsibilities, plan oversight, and fees. This could potentially lead to underutilization of the program.

This issue brief first provides some examples of decoupling approaches currently in use in the U.S. and elsewhere. Included among these examples are the Pooled Employer Plan (PEP) provisions of the *Setting Every Community Up for Retirement Enhancement* (SECURE) *Act* that allow defined contribution plan sponsors to join together in PEPs, broadening employers' options.[5] The issue brief then presents a summary of how decoupled plans can be consistent with the Academy's Retirement for the AGES principles[6] and concludes with a question-and-discussion section covering relevant issues and concerns.

Current Examples of Decoupling

State and Local Government-Based Retirement Initiatives

In recent years, a number of state and local governments[7] have adopted mandatory or voluntary initiatives in an effort to expand retirement coverage among private-sector workers. In a typical mandatory program, for example, a private-sector employer above a certain size operating in that state would be required to offer its employees the option to enroll in the state's program if the employer does not offer its own retirement plan. Participating employers would be responsible for collecting employee contributions via payroll deduction and remitting those contributions to the state program. However, employer contributions would not be required. The responsibility for maintaining the program and selecting administration and investment service providers would remain with the state. Many of these initiatives have been structured as automatic individual retirement account (IRA) or Roth IRA arrangements. In addition to expanding retirement coverage while minimizing employer roles and responsibilities, such programs are able to take advantage of economies of scale after achieving a critical mass. Some state programs allow self-employed and gig-economy workers to participate in the plans.[8] The effectiveness of these programs remains to be seen, especially with the availability of PEPs, as discussed below.

5 Prior to the SECURE Act, the existence of multiple employer plans provided some employers with an option for decoupling, but there were significant limitations to their availability and effectiveness. The SECURE Act allows a greater degree of decoupling for 401(k) plans; since the SECURE Act, further legislation has been proposed to allow a similar degree of decoupling for 403(b) plans.
6 See the discussion of the Academy's AGES principles later in this issue brief.
7 "State Initiatives 2021: More New Programs to Launch While Others Consider Action"; Georgetown University Center for Retirement Initiatives; 2021.
8 Certain state programs also permit small nonprofit organizations to participate in a state-sponsored qualified defined contribution plan, rather than sponsoring their own plan. Such a state-sponsored program would permit contributions by both employers and employees, in contrast to automatic IRA arrangements, which generally permit only employee contributions.

Pooled Employer Plans Under the SECURE Act

The SECURE Act includes a provision that has the potential to change saving for retirement in a fundamental way. Private-sector employer-sponsored retirement plans have historically been established and administered by individual employers. Exceptions have existed for related employers, employers whose employees are covered under a common collective bargaining agreement, or employers that have contracted with a Professional Employee Organization. Under the SECURE Act, unrelated employers will now be permitted to join PEPs. These defined contribution PEPs will be administered by Pooled Plan Providers (PPPs) operating under rules established by the U.S. Department of Labor (DOL). Though the intent of this provision of the SECURE Act is primarily focused on smaller employers without plans, another significant outcome may be further decoupling of the administration of retirement plans from the employers in general.

The Australian Superannuation Guarantee Program (Super)

This is a savings scheme wherein employers set aside contributions on behalf of their workers to provide for their retirement. Employers are required by law to make at least minimum Super contributions into a registered Super Fund of an eligible employee's choosing (or into an employer-chosen default Super Fund if employees do not make an election), referred to as Super Guarantee (SG). Penalties may apply if employers fail to meet the SG obligation, fail to properly offer a choice of Super Funds, or for other administrative violations.

TIAA

TIAA serves as the retirement plan for many universities and select not-for-profit employees/employers. Employers make contributions and direct employee contributions to TIAA. Participants can purchase a traditional or variable annuity, which pays out benefits for a lifetime. This benefit provides insurance protection, and TIAA acts essentially as a not-for-profit mutual insurer. The employer is neither a sponsor nor a financial guarantor.

Netherlands: Collective Defined Contribution (CDC) Plans

In these plans, employees earn benefits based on their compensation—essentially a career average formula under a traditional defined benefit (DB) plan. Benefits are paid as inflation-indexed lifetime annuities. There are no individual accounts. Rather, all contributions are pooled and invested together. In these respects, the plans appear to be traditional DB plans. Employees and employers each contribute a fixed percentage of compensation in order to fund these plans. The percentages are designed to target a funded ratio of 130%. Employers have no risk of higher contributions. There is a notable difference between these CDC plans and traditional DB plans. The risk of investment losses is borne entirely by employees and retirees. If the plan suffers losses, the governing board (with representation from employees, retirees, and employers) decides what adjustments will be made. Adjustments can include an increase to employee contribution levels, elimination of indexing on the benefits, and reductions in future years' benefit levels. Overfunding will go to the benefit of employees rather than reducing employer contribution levels.

Swiss Cash Balance Plans

These plans operate much like defined contribution plans, but have minimum investment guarantees and minimum interest rate and mortality standards for the conversion of account balances to annuities. Benefits are funded jointly by the employer and employee, with employer contributions required to make up at least 50% of total contributions. The plans are managed and administered by independent nonprofit foundations. The employer is responsible for tracking participant status and communicating it to the plan, as well as remitting employer and employee contributions. The plan foundation board is responsible for investment strategy (operating within certain legal constraints) and plan compliance with applicable legal and regulatory requirements. While the board is at least partially responsible for participant communication and plan design, the employer can communicate with participants as well, and half of board members are employer representatives.

Single-Employer U.S. Defined Contribution (DC) Plans

U.S. defined contribution plans do not exhibit any significant degree of decoupling. While most employers will utilize outside providers for certain functions—such as recordkeeping, compliance testing, investment management, and participant communication—and the outside provider may act as a fiduciary in some cases, the employer retains the ultimate responsibility for these functions as plan fiduciary. This may make some smaller employers reluctant to offer plans to their employees.

Comparison of Above Examples of Decoupled Plans

The functional responsibilities generally involved in the maintenance of a retirement plan include:

- **Participant Status:** Initial employee enrollment in the plan and updating employment status
- **Administration:** Processing of benefits, updating of vesting percentages
- **Remitting Required Contributions:** Facilitating the withholding of employee contributions and the transfer of funds from the employer to the plan provider
- **Compliance:** Maintaining plan document and compliance with other regulatory requirements, including government filings
- **Investments**: Selection of prudent investment choices and/or selection of qualified investment adviser; plan design may or may not allow investment choice by participant
- **Communication:** Provide information about investment options and account balances
- **Design**: Selecting plan provisions

The following table indicates who is primarily accountable for each of these responsibilities under each of the seven plan types noted above. In a decoupled plan, some of these responsibilities could possibly be shared by the employer, TPE, and employee/participant. The degree to which responsibilities may be shared will depend on the details of the arrangement.

	Program						
Functional Responsibility	**State & Local Initiatives**	**PEPs under SECURE Act**	**Australian Super**	**TIAA**	**Netherlands CDC**	**Swiss Cash Balance Plans**	**U.S. Private Sector Single Employer DC**
Participant Status	Employer	Employer	Employer	Employer	Employer	Employer	Employer
Administration	TPE	TPE	TPE	TPE	TPE	TPE	Employer, TPE
Remitting Required Contributions	Employer	Employer	Employer	Employer	Employer	Employer	Employer
Compliance	TPE	TPE	TPE	Employer, TPE	TPE	TPE	Employer, TPE
Investments	TPE, Supervi-sory Entity	Employer, TPE	Employer	Employer, TPE	TPE	TPE	Employer, TPE
Communication	TPE	TPE	TPE	TPE	Employer, TPE	Employer, TPE	Employer, TPE
Design	Supervisory Entity	Employer, TPE	Supervisory Entity	Employer	Employer	Employer	Employer

Legend for Color Coding:
- Employer has primary responsibility, even if outsourcing tasks to an outside provider
- Employer shares responsibility with another party/entity
- Primary responsibility lies with a party/entity other than the employer

Decoupling in Defined Benefit Plans

The plans analyzed above are for the most part DC plans. DC plans may be better candidates for decoupling than DB plans. The main reason is the inherent design of DB plans. DB plans generally require that plan sponsors assume financial responsibility beyond any fixed annual contribution levels. For decoupling to work effectively, it is important that employers have a known financial exposure.[9] For example, plans that are structured to pay out lifetime income would require adjustments to mitigate the possible need for additional employer contributions, such as benefit adjustments in a variable defined benefit plan. See the issue brief *New Retirement Plan Designs: Degrees of Risk Sharing* for more thoughts on this topic.

There are already several examples of partially decoupled DB plans. The most well-known is with the U.S. multiemployer plan system, which covers employees in the same union who work for different employers. Participating employers have very few administrative responsibilities, other than to provide TPEs with employee data and contributions. Most other plan functions such as investment management, hiring of providers, etc., fall to a board of trustees. These plans provide many economies of scale, but generally do not shield individual employers from financial exposure. Employers make pre-negotiated fixed contributions to the plan on behalf of their plan members. These contribution levels are periodically reset based upon collective bargaining. When a plan is poorly funded, there can be large required contribution increases. Should an employer leave the plan (voluntarily, or if the plan is being dissolved), it is generally required to pay its share of any underfunding of the plan. If the employer is unable to meet this obligation, the other employers in the plan may need to assume it. In some cases, the plan may become insolvent and the Pension Benefit Guaranty Corporation may need to provide financial support.

Other decoupled DB designs are found in public employee plans in states, counties, and municipalities. Many states have statewide municipal retirement systems in which local governments may enroll their employees in lieu of establishing their own pension plans. These systems typically allow employers to select among different levels of benefits for their employees, with associated differences in contribution requirements.[10] Statewide municipal systems allow for economies of plan administration and investment activity

9 While a DB plan sponsor could potentially purchase annuities from an insurance company on a periodic basis to cover DB accruals, thus eliminating further financial exposure for those accruals, the cost of purchasing annuities could vary significantly from year to year and the plan sponsor would still retain primary responsibility for the design and administration of the plan.

10 As an example, see the Academy's *Retirement for the AGES Assessment—Maine Participating Local District Consolidated Retirement Plan*

that might be difficult to achieve in a standalone municipal pension plan. Additionally, through their statutory authority, the states have the ability to enforce a greater commitment to funding by their municipalities, which has sometimes been lacking in plans that are only under the control of a municipality.

Social Security provides another example of decoupling in a DB retirement system. Employers' responsibility under the system is to remit payroll taxes to the federal government. This program is, however, different from the others noted here in that it is mandated and administered by the federal government.

Decoupling and the AGES Principles

In January 2014, the American Academy of Actuaries published a public policy monograph, *Retirement for the AGES* (**A**lignment, **G**overnance, **E**fficiency, and **S**ustainability). This monograph lays out a framework for assessing employer-based retirement programs, or policy changes that would affect them, to understand how well they meet the needs of each of the stakeholders. The AGES principles are as follows:

(A) Alignment—Retirement income systems work best when stakeholders' roles are aligned with their skills. Important tasks, such as financial analysis, investment management, and retirement plan administration, should be the responsibility of those who have the knowledge and experience to perform them well.

(G) Governance—Making and implementing good decisions are essential for successful retirement plans. Good governance helps balance the complex needs of various stakeholder groups, as well as oversees significant administrative and investment functions.

(E) Efficiency—Risk pooling, accurate pricing, appropriate use of guarantees, and other financial techniques should be adopted or incorporated to ensure that a retirement income system is efficient and maximizes income while avoiding excessive risk to stakeholders.

(S) Sustainability—Roles and skills, good governance, and financial efficiency should be structured to support a sustainable retirement income system that is able to withstand the financial shocks of recessions or times of extraordinary inflation.

As noted below, certain features of decoupled plans can be consistent with these principles. Note that decoupling may have value for both employers and employees. The letters in parentheses relate to the AGES principles as noted above:

Employers

1. *Possibly lower administrative costs:* Outsourcing of administrative responsibilities to a provider that is in the business of administering plans will likely reduce overall costs of administration as a result of economies of scale. (A, E)

2. *Possibly lessen internal administration efforts:* Under a decoupling approach, much of the routine plan administration could be transferred from the employer. This allows employers to focus on their core businesses. (A, E)

3. *Potentially lessen fiduciary liability:* TPEs can take on the legal responsibility for some of the operational functions under a plan. (A, G, E)

Employees

1. *Pricing:* Through the economies of scale, TPEs may be able to offer institutionally priced investment options and insurance product pricing. The lower the costs, the greater the potential for larger ultimate benefit accumulations. (E)

2. *Access to retirement plans through an employer:* Lower employer costs and administration efforts and liabilities will likely increase the attractiveness for smaller employers to participate. (S)

3. *Possibly easier access to education and advice:* Many employers do not advise their employees about the finances of retirement security at both the accumulation and decumulation stage. TPEs will likely consider this a key feature in their offerings to attract clients. (A)

4. *Potentially providing employees with greater access to retirement income solutions:* Many employers (especially smaller ones that may not have access to unbiased advice) will find selecting appropriate retirement income options very challenging. Larger TPEs will likely be better suited to provide this critical service to employees of those participating in the TPE. (A, S)

Questions and Discussion Regarding Decoupling

1. What will the government regulations require for TPEs? How will ERISA rules apply? A TPE, depending upon its role, may be expected to act in a fiduciary capacity serving the best interests of the plan participants. Disclosure items should be robust and easy to understand.

2. What, if any, limitations will be placed on investment options offered? Will low-cost, passive investment funds be required as an option? Modern design features in retirement savings plans have focused on making it easier for participants to save enough money and select appropriate investments. Providing a limited number of low-cost, diversified investment options could help participants avoid several tendencies that are common among individual investors: failure to consider impact of high fees, "churning" their investments, and selecting overly conservative investments.

3. Does a TPE offer a range of retirement income distribution options, including both insured products and those based on structured withdrawal strategies?[11] A larger TPE might be better able to offer a range of retirement income distribution options than an individual employer.

4. How will an employer select a TPE (or multiple TPEs)? Selecting a TPE can be a challenge, especially for smaller employers. Many employers might look to independent experts to help review their options.

5. Depending on the functional responsibilities of a TPE, does it offer education and advice to employees? In giving specific advice, will a fiduciary standard be required? Individuals often find long-term retirement planning complex and very difficult, and often look to and rely on their employer to provide education and a clear path to retirement. TPEs that provide education and advice to employees would ideally include education about retirement planning and unbiased advice when it comes to selection of investments. Therefore, requiring a fiduciary role and responsibility for those entities providing advice would be important.

11 For example, use of the 4% rule or payout of required minimum distributions.

6. How will TPEs attract the interest of one-person businesses in the gig economy who may jump from project to project? Gig workers are, almost by definition, on their own for their livelihood, financial wellness, and retirement savings. Several states have established state-based retirement savings programs, and some have allowed self-employed and gig workers to join. Those states implemented outreach initiatives targeting gig workers. It would be very beneficial if PEPs or other decoupled arrangements establish an outreach program and a clear path for gig workers to participate as individuals.

7. How will private-sector plans that utilize TPEs to decouple functional responsibilities compare to the state-based programs that are currently being established? Select states, as well as at least one municipality, have recently enacted their own retirement initiatives (such as automatic IRA arrangements), attempting to address retirement coverage and adequacy concerns.[12] In some of these, the programs are required to be offered by employers that do not sponsor a workplace retirement plan. Many of these programs are limited to an IRA structure and its associated contribution limits. Can TPEs offering lifetime income solutions use longevity risk pooling directly, or must they use insured annuity products? In general, direct longevity pooling is not permissible in DC plans in the current legal and regulatory environment. However, should this change in the future, TPEs could be well-positioned to offer such solutions. Ultimately, the impact of mortality experience that is different from expected mortality will most likely be borne by plan participants, because employers might be reluctant to expose themselves to an unknown level of risk. As a result, TPEs may hold an attraction if they minimize employer liability exposure.[13]

8. Does a TPE serve as a vehicle to consolidate retirement accumulations from prior plans? The issue brief *Retirement Security Challenges: Portability and Retirement Income* outlines the challenges employees face in trying to manage accumulations from multiple plans of their former employers. The ability to easily consolidate and manage such savings could reduce the likelihood that workers will lose track of their savings or use them for nonretirement purposes.

12 "State Initiatives 2021: More New Programs to Launch While Others Consider Action"; op. cit.
13 See Academy issue brief *New Retirement Plan Designs:Degrees of Risk Sharing*.

9. Will plans utilizing TPEs for decoupling totally replace traditional single-employer plans? Such arrangements are likely to appeal to employers that want to offer retirement benefits to their employees while eliminating or reducing the employer's involvement (e.g., administration, communication, cost and risk of operating the plan, fiduciary responsibility). For example, PEPs under the SECURE Act are expected to gain some popularity.[14] Most likely, some large employers (in both the private and public sector) with existing plans custom designed for their own needs will continue to maintain those plans, as those plans may have relatively low administrative costs and low-cost investment options.

Conclusion

Approximately one-third of all private-industry workers in the U.S. lack access to an employer-sponsored retirement plan. These workers are often employed at organizations that are small and lack the financial and human capital resources to sponsor a retirement program. In addition, businesses of all sizes may prefer to focus their energies on their business proposition rather than administering benefit programs. In this environment, shifting retirement plan responsibility and related liability to a third party can be a sound business and risk management approach.

Outsourcing some of the functional responsibilities for a retirement program could provide benefits in cost and risk reduction as well as the ability to offer options and features that otherwise would not be possible or would be too costly. Single-employer plans will continue to be a viable option for many employers; however, decoupled plan structures, such as PEPs under the SECURE Act and state and local government-based retirement initiatives, have expanded the options available and provide new opportunities to private-sector employers.

14 See Academy issue brief *Pooled Employer Plans—Employer Considerations*.

In July 2019, the American Academy of Actuaries Retirement System Assessment and Policy Committee published an issue brief titled *National Retirement Policy & Principles*, which discussed the increasing need for a comprehensive national retirement policy based on certain guiding principles. This initial issue brief has been followed up by four additional papers in the series:

- *Retirement Security Challenges: Portability and Retirement Income* (April 2020)
- *New Retirement Plan Designs: Degrees of Risk Sharing* (October 2021)
- *Retirement Policy: Potential for Changing Roles of Employers in Retirement Programs* (October 2021)
- *Retirement Policy: Aligning Plan Design With Effective Employee Engagement* (March 2022)

Taken together, these issue briefs lay out guiding principles that policymakers can look to as they consider the establishment of a comprehensive national retirement policy.