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Plan Sponsors Should Be Intentional When Adding Managed Accounts

Standard benchmarking may not yet cover such offerings, but plan sponsors can monitor participant satisfaction, plans' stated objectives.

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Managed accounts are growing in popularity. According to data from retirement consultant Mercer, 48.8% of defined contribution plans offer a managed account solution to plan participants, a figure that has grown by 9% over the past five years. Mercer data suggests that plan sponsors are looking to managed accounts to help personalize retirement plan offerings and to provide important services like access to financial advice.

Despite the uptake in adoption, there are still many questions that have to be answered to implement a managed account offering effectively and to be able to measure it over time. Benchmarking can be challenging because by their nature managed accounts are designed to be highly tailored to an individual's needs, making an apples-to-apples comparison across product offerings may not always be feasible. Sources say that plan sponsors have the best chance at success if they identify from the beginning and work with service providers to deliver on those outcomes and provide adequate documentation.

Striking The Right Balance

Deciding to offer a managed account solution presents a unique set of fiduciary challenges. Managed accounts are typically more expensive than other offerings like target date funds and can cost more than what participants would pay using a self-directed brokerage account window. Managed accounts are also highly customizable and can be used to offer anything from financial wellness programs to supporting dynamic QDIA programs. Because of this level of personalization, plan sponsors may have difficulty with benchmarking if comparable providers offer some, but not all, of the same solutions or capabilities.

Holly Verdeyen, Chicago-based partner and U.S. defined contribution leader at Mercer, tells PLANSPONSOR that the plan sponsors she works with typically start evaluating managed accounts because participants ask for them, but those participants often represent a vocal minority.

"Whenever plan sponsors start looking at making adjustments to the plan, they have to balance the needs of all types of participants," she says. "Effective evaluation of managed accounts includes more than just looking at fees. Plan sponsors need to consider what the participation rate might be as well as the performance of any investment solutions included in the offering."

Verdeyen notes that the type of managed account provider being considered can have an impact too. Mercer data shows that recordkeepers are increasingly offering their own managed-account solutions that are designed to fit into existing platforms. Verdeyen says that while these can look like an easy option on the surface,

"There are going to be differences between these proprietary managed accounts and what you might see from a retirement plan adviser. They could be focused on different services or the user experience might be different," she says. "Cost is an issue as well because there are a number of complexities with managed accounts. Some features may be marketed as low or no cost, but nothing is ever really free. Our advice to clients is to make sure they are looking closely at what's available and comparing it to other providers."

Identify Desired Outcomes

Plan sponsors should also consider the goals of their managed account offering. A recent report from Cerulli Associates shows that 52% of plan sponsors view managed accounts as a way of providing participants with access to financial advice, but that's not the only reason to use them.

"Financial planning and wellness features, and the ability to speak with an adviser, may have a meaningful impact on participants' financial outcomes. Nevertheless, plan sponsors may need to employ different performance evaluation approaches to quantify their impact," wrote Shawn O'Brien, director of the retirement practice at Cerulli Associates in the report.

Adrian Miguel, director, communications consulting, participant education and advice for Schwab Workplace Financial Services, adds that managed accounts can increase savings rates among participants.

"Our data shows that when individuals go through a consultation with a professional, we see that about 60% of those participants end up saving more than those who do not. The average yearly increase in savings is nearly 4%," Miguel says. That outcome may be powerful enough to justify a higher cost.

Verdeyen agrees. If the goal is to improve savings and add customization, Verdeyen says, then being able to offer professionally managed solutions that take into account a participant's entire financial picture might be more valuable than asking them to self-select into a target date fund based only on a projected retirement year.

Documentation and Communication

Because of the high level of customization available through managed accounts, both Miguel and Verdeyen say it's important for plan sponsors to have a well-documented case for their decisions.

Schwab offers fully open architecture with its managed account offering and can integrate with 3(38) fiduciary services offered through Morningstar and other providers. "We offer that because we do understand the reality plan sponsors face when it comes to making choices about their plans," Miguel says.

Ongoing documentation is also critical for plan sponsors that choose to offer managed accounts in part because benchmarking them over time will require more work than other parts of the retirement plan offering. Marcia Wagner, founder and managing partner at Wagner Law Group in Boston says there is no optimal way to benchmark managed accounts.

"Plan fiduciaries may begin with comparing the returns of the managed accounts with the returns of target date funds, but that approach is incomplete because it fails to take account of the personalized nature of the managed account structure," she explains. "For the same reason, the measurements that are generally used by advisers to monitor the performance of funds such as their projected returns, historical returns, volatility, and Sharpe ratios do not align exactly with managed accounts. There may also be a sort of inherent value, in that managed accounts represent an intermediate option between QDIAs, such as target date funds, for participants who want to leave investment responsibility entirely to others, and those plan participants with self-directed accounts who want to have investment responsibility."

Plan sponsors may end up using these measurements as part of an overall process. At a minimum they provide insight into investment performance on a relative and ongoing basis. Still, Wagner says two big metrics plan fiduciaries can map to are participant satisfaction with the offering and whether or not managed accounts are delivering on the goals that plan sponsors identified when they initially chose to offer them. Wagner suggests that fiduciaries can do a demographic study to see if participants across the entire plan are deriving a benefit from managed accounts, which could provide a more precise result than simply looking at investment metrics.

Verdeyen adds that in addition to having a clear documentation, plan sponsors should consider updating their communication and engagement strategies to make sure participants are aware of the full scope of what the managed account can do for them as well as any additional costs.

"There is a bit of an inherent tension here," she says. "Managed accounts have grown in defined contribution plans because there are benefits. But they have also caught the attention of attorneys and litigators looking for any breach of fiduciary duty. So it's important for plan sponsors to take their time and be clear about why they made the choices

they made, whether they choose to include managed accounts or not. All of those decisions should also be communicated to participants."

Tags investment performance, Managed Account, QDIA, retirement plan fiduciary duties, Special Coverage: Plan Benchmarking, Target Date Fund

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