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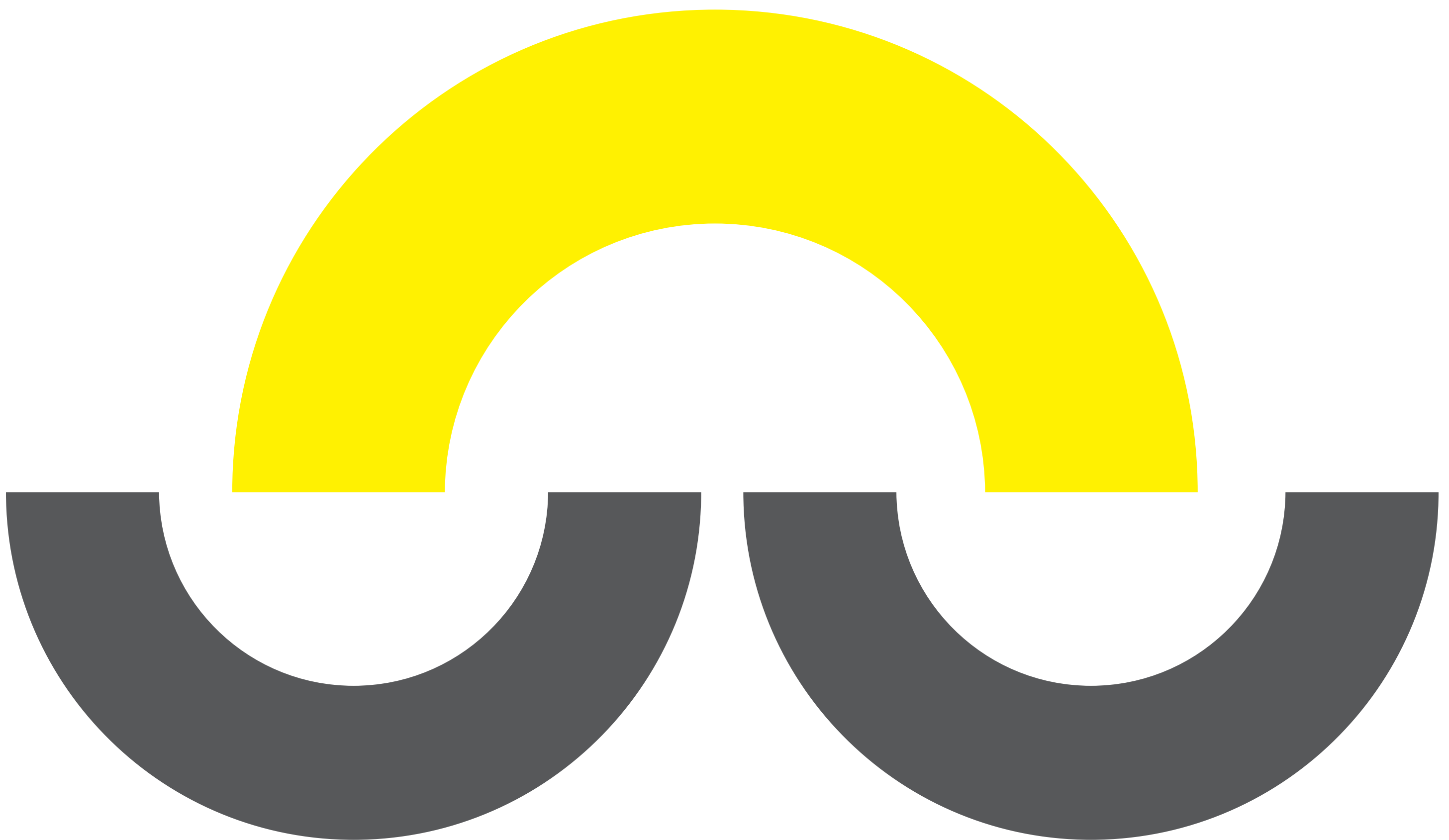
Benchmarking 401(k) rollover behavior



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Participants in retirement plans in the U.S. receive generous tax incentives from the federal government to encourage saving for retirement. As taxpayers, both employers and individuals have a vested interest in ensuring these dollars are used for their intended purpose—and not to pay inflated fees for services.

Rolling retirement assets out of employer-sponsored plans and into individual retirement accounts (IRAs) can place hard-saved dollars at risk, which has resulted in the increased scrutiny of rollover practices.

The attention on rollovers has, in part, been fueled by the Department of Labor's fiduciary regulation that underscores the importance of providing trusted and unbiased guidance to individuals when they are making the key decision about what do to with the savings in their company's retirement plan. Additionally, a 2013 report from the Government Accountability Office[1] (GAO) condemned practices that appear to steer individuals to roll over their 401(k) balances to IRAs.

In light of this increased attention, sponsors of large retirement plans are asking some fundamental questions:

- **Should plan sponsors monitor the IRA rollovers from their plans? Why or why not?**
- **What are "good" reasons for participants to roll 401(k) balances into IRAs?**
- **How can plan sponsors know if their participants are subject to undue influence or steerage with respect to rollover decisions?**
- **Who is responsible for assessing rollover behavior?**

As the largest independent recordkeeper of defined contribution plans in the U.S., Alight Solutions does not promote any particular IRA provider or product. Workers who leave the plans we administer receive unbiased decision support across all their rollover choices, with no single provider or option receiving preferential treatment.

Our business model enables us to observe the choices people make when they aren't steered toward any one product or solution by their plan administrator. It is through this perspective that we attempt to answer the questions above.

Should plan sponsors monitor the IRA rollovers from their plans? Why or why not?

In short, yes. Plan sponsors should be monitoring the amount of IRA rollovers from their plans, the destination of the rollovers and the revenue generated from those rollovers. After all, plan sponsors have the fiduciary responsibility to act in the best interests of their plan participants. Any measure that could sway people's behavior should be carefully reviewed to ensure that it does not run counter to their best interests and create undue risk to the plan—especially if employee rollover behavior results from decisions made by plan sponsors, such as providing access to participants via a recordkeeping relationship or onsite education.

Currently, service providers must provide fee and revenue data to plan fiduciaries so they can make informed decisions. However, rollover revenue has remained largely out of the requirements, making it difficult for plan sponsors to identify any potential conflicts of interest between recordkeepers and IRA providers.

Usually, moving retirement assets from a large employer plan with low fees to an IRA will add additional costs for participants. Do participants fully understand this? Plan sponsors could be held accountable if the answer is no.

What are "good" reasons for participants to roll 401(k) balances into IRAs?

There are three primary considerations for people who are deciding whether to roll their 401(k) plan balance into an IRA, and depending on the specifics, a rollover to an IRA may actually be a "good" choice.

1. **Distribution and/or investment options.** Some 401(k) plans do not allow participants to take a partial withdrawal or installment payments from the plan.[2] In these instances, it can be a tax advantage for retirees to roll their plan balance into an IRA and avoid cashing out so that they can retain distribution flexibility. Some plans also do not offer the investment flexibility desired by participants to meet their asset allocation goals. Rolling assets into an IRA could provide this flexibility.

2. **Fees.** Small 401(k) plans may have high fees, but generally, as the size of the 401(k) plan increases, the amount charged to participants decreases.[3] This is primarily because large plans have institutional purchasing power for investment options—which translates into lower fees for large 401(k) plans than for IRAs. As fees compound over time, individuals should compare the costs of IRAs to those of 401(k)s before considering their rollover decision, as moving assets from their institutionally priced 401(k) plan into an IRA can potentially drive up fee expenses, which would eat into available funds saved for retirement.

3. **Asset consolidation.** For individuals who are no longer able to participate in a 401(k) plan, IRAs can be a natural place to bring together multiple accounts that are earmarked for retirement. As workers move from job to job or in and out of the workforce, an IRA can be a steady depository for retirement assets. This consolidation makes it simpler for people to see their total retirement nest egg and makes it easier to select, monitor and rebalance investments.

Whether or not a decision is "good" is highly subjective—the key is to help people avoid making decisions that are uninformed or misinformed. In these circumstances, rollovers are at greater risk of being "bad."

Annual IRA rollover percentage less than or equal to	Percentage of plans
25%	**95%**
20%	**88%**
15%	**74%**
10%	**34%**
5%	**13%**

How can plan sponsors know if their participants are subject to undue influence or steerage with respect to rollover decisions?

While there are sound reasons for some people to roll savings plan accounts into IRAs, how much is too much? And how do you know when people are being steered toward a decision? Large plan sponsors with "good" rollovers should feel confident stating the following:

1. **The amount of assets rolled over to IRAs is within industry norms.** We analyzed three years of data from more than 20 very large 401(k) plans that have *no* facilitation or encouragement of one single IRA provider over others. Our analysis shows that, on average, 13% of distribution-eligible balances are rolled over to IRAs in any given year. The amount of rollovers from a plan can vary from year to year and from plan to plan, but usually fewer than 15% of distribution-eligible dollars are rolled into IRAs in any year.

   Plan sponsors should compare their IRA rollovers to benchmarks such as this. Furthermore, viewing deviations in the context of plan design, plan fees and worker tenure can shed light on rational reasons why rollovers might be higher or lower than this benchmark and whether the results are influenced by steerage.

2. **There are diverse destinations for IRA rollovers.** While some providers receive more rollovers than others, plan sponsors should expect to see a wide range of rollover destinations. We found that more than 2,000 IRA providers received distributions between 2014 and 2016 in the plans we analyzed. Our analysis also showed that the top IRA destination received 16% of all IRA rollover dollars. Even though this was much more than the second-ranked destination, it still represented less than one out of every six dollars rolled over to IRAs.

Destination rank	Percentage of IRA rollovers
Provider 1	**16%**
Providers 2–5	**26%**
Providers 6–10	**22%**
Providers 11–25	**18%**
Providers 25–50	**9%**
Providers 50-2,000+	**10%**

Benchmarking the destination percentages is perhaps even more important than monitoring the overall level of rollovers. If any providers are receiving more than a reasonable percentage of rollovers, it could very well be considered steerage.

Finally, revenue from rollovers should be considered. Revenue and fees from rollover dollars should be compared to revenue received from the providers for other services provided to the plan. Industry benchmarks are not available, but any significant revenue creates potential conflicts of interest. It is important for plan sponsors to understand those conflicts to be able to manage them, and to ensure participants are not subject to undue influence as a result of those conflicts.

Who is responsible for assessing rollover behavior?

Plan sponsors are responsible for monitoring the rollovers from their plans to the extent those rollovers are facilitated by a provider they choose. Recordkeepers that have retail IRA products may have conflicts of interest and incentives for participants to roll 401(k) balances to IRAs, so they alone cannot be relied upon for the oversight.

We recommend plan sponsors take the following steps to assess the rollovers from their plans:

1. **Ask your recordkeeper for the annual percentage of rollovers from your plan.** Examine this data on both a headcount and asset-weighted basis.
2. **Compare the amount being distributed each year to the levels shown in this paper and other benchmarks.** If your data is an outlier, be able to justify the discrepancy.
3. **Inspect the destinations for IRA rollovers.** Are there sound reasons for the top destinations receiving more than others?
4. **Review communications to plan participants that relate to rollovers.** Are there any printed materials, call center discussions or face-to-face meetings that can be interpreted as encouraging participants to roll balances to IRAs?
5. **Review revenue streams from the rollovers.** To the extent your rollover results are outside the benchmarks and revenue streams suggest a conflict, carefully review the potential sources of persuasion—call center discussions, online and mobile experiences and embedded guidance or education—that could be creating undue influence.

If it seems too good to be true . . .

It is not uncommon to have an IRA provider offer to complete all the paperwork for an IRA rollover. Others will offer monetary incentives for a rollover, with some offering thousands of dollars depending on the amount rolled over. Knowing that there is no such thing as a free lunch, participants should realize that these incentives must be paid for in some way.

Conclusion

What people choose to do with their carefully saved retirement money when they leave or change jobs can have a significant impact on their future financial security. Employers are uniquely positioned to help their current and former employees make smart, informed decisions with their long-term goals and interests at heart. Monitoring rollovers and addressing if, where and how retirement money is being steered is a low-cost, low-effort way to help ensure a secure retirement for Americans.

Endnotes

1 U.S. Government Accountability Office, "Labor and IRS Could Improve the Rollover Process for Participants," March 2013. The report can be found at www.gao.gov/products/GAO-13-30.

2 Our analysis of nearly 300 plans shows that 18% of plans have a lump sum as the only distribution option for plan participants.

3 Deloitte Consulting and ICI, "Inside the Structure of Defined Contribution/401(k) Plan Fees, 2013: A study assessing the mechanics of the 'all-in' fee."

About Alight Solutions

As the leading provider of benefits administration and cloud-based HR and financial solutions, we enhance work and life through our service, technology and data. Our 22,000 colleagues across 14 global centers deliver an unrivaled consumer experience for our clients and their people. We are Alight. Reimagining how people and organizations thrive.

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