

NAGDCA ANNUAL CONFERENCE 2009

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**Plan Retirees:  
The Next Horizon of Defined  
Contribution Plan Administration**

Moderator:  
Ralph Marsh, City of Houston (TX)

Speakers:  
Ann Fuelberg, State of Texas  
Stacy Schaus, PIMCO

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**Ann Fuelberg**

Employees Retirement  
System of Texas

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## ERS helps members to prepare

Retirees need full spectrum of programs and services to face 'economics of retirement'

- Flexible programs with options
- Financial resources and education
- Health and welfare programs

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## ERS programs include

- Defined benefit pension
- Group insurance benefits, including retiree health, dental, life insurance and long term care
- Section 125 reimbursement accounts
- Texa\$aver Deferred Compensation program

State of Texas employees also pay into/receive Social Security benefits

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## Texa\$aver Program

- Offers both 401(k) and 457
- Has no employer match
- Is mandatory for state agency employees at 1% of salary (as of January 1, 2008)
- Includes personal brokerage account, target date funds and core investment options
- Provides basic investment advice to all with opportunity to upgrade for additional fee

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## Experience

Over the past decade, the State of Texas has experienced:

- an 11% decline in the number of active employees
- a 59% increase in the number of retirees
- a 900% increase in the number of retirees who have returned to state employment after retiring.

In 10 years, ERS' monthly annuity payroll has grown 226%, from \$50 million to \$113 million



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## Background

### ERS Pension Plan Demographic Changes Since FY2000

Retiree Trends	2000	2008	% Change
Number of Retirees	45,843	72,678	+ 58.5%
Number of Return-to-Work Retirees	553	5,522	+ 899%
Average Annual Annuity	\$15,412	\$18,611	+ 20.8%



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## Many factors will force ERS members to work longer

- Cost increases in defined benefit plan forced changes designed to encourage longer careers
  - Discourages returning to work
  - Changes benefit calculations for employees hired after September 1, 2009
  - Increased mandatory employee contribution
- Defined contribution investment losses in personal accounts



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## Retirees need flexible distribution options

### Texa\$aver distribution options:

- Lifetime annuity
- Partial lump sum
- New feature will let retirees specify source of distributions – particularly crucial in volatile markets

ERS supported lifting the federal mandate for distribution at age 70 ½ this year



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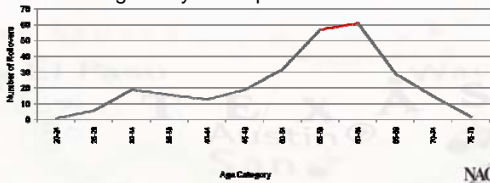
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## Research

Conducting research on rollover trends out of the Texa\$aver program to see how we might serve employees better

-rollovers peak around age 55-64.

Marketing campaign targets members with message “stay in the plan” at termination



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## Paying for health and long term care in retirement is crucially important

State of Texas currently pays full premium cost for qualified retirees and covers 50% of dependent premium cost

- Cost containment programs, aggressive contracting, coordination of benefits, and taking advantage of programs such as the federal Medicare Part D subsidy have kept trends below national trends
- May be able to protect current retirees, but health insurance cost is not sustainable for the long term
- State offers group long term care program for retirees and family members



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## ERS educates members and retirees

Financial messages focus on:

- the “three-legged stool” – social security, state pension, personal savings
- the importance and responsibility to have personal savings

This year, we added messages recommending patience and self-control during the market decline



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## ERS educates members and retirees

- Revamped Statement of Retirement Benefits which now includes multiple annuity estimates to show employees how their annuity increases each year they work past their first retirement eligibility
- Timed the statement to roughly coincide with Social Security annual statement
- Make the statement accessible online at any time



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## ERS educates members and retirees

Equally important are messages about health care costs

- the value of state health benefits
- the probability of increasing out of pocket costs and cutbacks in coverage
- the importance of maintaining health
- how to take advantage of the health plan's wellness tools

Messages include that state health benefits are not guaranteed and could change at any time.



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## Plan sponsors should assist members to face economic reality

- Don't sugarcoat the future
- Set expectation of longer working careers
- Don't ignore the impact of declining health and health care costs
- Don't forget to plan for long term care expenses
- Provide full spectrum of investment products for different levels of investors
  - ERS offers both a brokerage account and target date funds
- Make saving for retirement easy for members
- Communicate early and often on key messages



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Stacy Schaus

PIMCO

The information from this section was provided by PIMCO. PIMCO has not independently verified any information prior to this section and is not responsible for the accuracy or the completeness of such information.

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Ask yourself as a plan sponsor...

***Should they stay or should they go?***



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### Why Encourage Employees to Stay or Go?

#### Why Encourage Staying:

- Lower cost of investment management for all participants
- Spread the cost of administration to a larger base
- Increase revenue sharing from mutual fund companies
- Provide a **lower** cost savings program to retirees and other past employees—you care!

#### Why Encourage Leaving:

- Investment cost reduction appears unattainable
- Administrative costs may rise if they stay
- Continued connection with past employees may be undesirable—potential liability?



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### If you want them to stay...consider

- Structuring plan to manage risks faced in retirement
- Increasing distribution flexibility
- Adding retirement income products
- Allowing consolidation of assets within the plan
- Providing guidance and tools to encourage savings and show retirement income picture



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### Help manage risks retirees face...

- To reduce help volatility, market risk and inflation risk, consider:
  - Blending asset classes and styles,
  - Adding diversifying assets such as Emerging Markets
  - Offering inflation protection via TIPS, Commodities and Real Estate
- To address market and longevity risk:
  - Adding or considering a retirement income option product:
    - 78% of DC Consultants believe their clients are somewhat to highly likely to add a guaranteed income product in the next two years<sup>1</sup>
    - Guaranteed minimum withdrawal benefit products are of greatest interest to their clients<sup>1</sup>

<sup>1</sup> SOURCE: PRIMO DC Consultant Survey 2009  
Please refer to Appendix for additional risk information.



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## Help reduce risk by blending assets and adding inflation protection...

REAL GROWTH	High/Rising	<p><u>Best:</u> Stocks</p> <p><u>Mixed:</u> Commodities &amp; Nominal Bonds</p> <p><u>Worst:</u> ILBs</p>	<p><u>Best:</u> Commodities</p> <p><u>Mixed:</u> Stocks &amp; ILBs</p> <p><u>Worst:</u> Nominal Bonds</p>
	Low/Falling	<p><u>Best:</u> Nominal Bonds</p> <p><u>Mixed:</u> Stocks &amp; ILBs</p> <p><u>Worst:</u> Commodities</p>	<p><u>Best:</u> ILBs</p> <p><u>Mixed:</u> Commodities &amp; Nominal Bonds</p> <p><u>Worst:</u> Stocks</p>
		Low/Falling	High/Rising
		INFLATION	

Refer to Appendix for additional risk information.

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## Offer distribution flexibility...

	Percent of Plans Offering Payment From	Average Percent of Participants Electing*
Lump Sum	100%	89%
Installment payments	52%	8%
Partial Distributions	41%	19%
Annuity	15%	3%

\*When form of payment is available

SOURCE: Hewitt Associates Trends and Experiences in 401(k) Plans, 2007.

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## Provide retirement income programs...

- Benefits:
  - Lower pricing or higher payouts (3-9% potentially via annuity purchase platform)
  - Fiduciary oversight of investments or guarantee income product offerings
  - Objective education and support of programs
- Challenges:
  - Employer concern with fiduciary oversight or program selection
  - Cost or liability concern with retirement counseling
  - Competition for retirement assets given retail economic model

Refer to Appendix for additional risk information.

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### Most attractive types of products....

How attractive are the following guaranteed income products?	Total	Percentage
Lifetime income (guaranteed minimum withdrawal benefit)	26	84%
Fixed annuity	20	65%
Payment-stream product that pays out earnings and/or principal (3 to 7 percent, without income or longevity insurance)	11	35%
Longevity insurance	10	32%
Variable annuity	8	26%
Other (e.g., laddered TIPS, target date funds with insurance wrapper, immediate variable annuities)	3	10%
Capital-market derivative or non-insured principal-protection strategy	2	6%

n=31

SOURCE: PIMCO Survey Highlights 2009




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### Guarantee adoption may be slowed by plan sponsor concerns about....

What are the primary concerns that would stop your clients from offering guaranteed products?	Total	Percentage
Insurance company default risk	27	84%
Cost	23	72%
Transparency	21	66%
Fiduciary oversight	19	59%
Insufficient government support (e.g., safe harbor, regulatory clarity)	13	41%
Lack of participant demand	9	28%
Monitoring/Benchmarking concerns	6	19%
Other (e.g., liquidity, portability, administrative issues, product immaturity, communication difficulties)	5	16%
Selection criteria	3	9%

n=32

SOURCE: PIMCO Survey Highlights 2009




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### Allow consolidation of assets...

- Enable retirees to roll in outside assets into DC plan or deemed IRA
- Welcome spousal accounts to roll in as well
- Consider brokerage window to increase ability to hold funds and individual securities (e.g., stocks, bonds and ETFs)




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