Target Date Funds for Public Safety Plans

NCPERS 2018 Public Safety Conference

Jeff Nipp, CFA, CAIA

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Topics

- Growth of Target Date Funds
- Specific Public Safety Plan Issues Regarding Target Date Funds
- Considerations for Plan Participants
- Considerations for Plan Sponsors
- Considerations for Investment Managers
Growth of Target Date Funds

- TDFs First Developed in Early 1990s

- Pension Protection Act (2006): TDFs can be Qualified Default Investment Alternative (QDIA)

- Morningstar: TDF Assets Exceeded $1 Trillion in 2017

- Pensions & Investments: TDFs >20% of P&I 1000 DC Plan Assets

- Cerulli Associates: TDFs Expected to be Largest DC Plan Allocation by 2020, and to Receive 85% of Contributions by 2021
TDF Issues for Public Safety Plans

Example: Morningstar TDF Index Glidepath

- Typical Target Date Fund Retirement Age is ~65, but Public Safety Retirement Age is Often ~50-55
- PPA (2006): No Penalty on Lump-Sum Payments from DB Plans for Public Safety Employees Age 50+
- Defending Public Safety Employees’ Retirement Act (2016): Wider Definition of Public Safety Employee; No Penalty for Withdrawals at 50+ from Govt. DC Plans
- Assets Must Stay in the Plan—No Rollovers

Source: Morningstar.
Considerations for Plan Participants

J.P. Morgan Asset Management: Two Types of DC Plan Risks

- Participant-Controlled Risks (Plan Design)
  - Participant User Risk
  - Accumulation Risk
  - Withdrawal Risk

- Participant-Experienced Risks (Plan Investments)
  - Market Risk
  - Event Risk
  - Interest Rate Risk
  - Inflation Risk
  - Longevity Risk
Considerations for Plan Participants

- Do I have a DB Plan? Will I receive Social Security?
  - DB/SS payments can be considered to be a fixed income allocation
  - Such payments could argue for use of more aggressive (longer-dated) TDFs
  - Required DB Plan contributions may limit ability to contribute to DC Plan

- Do I plan to continue working (in a non-Public Safety job)?

- When will I need the DC Plan money?

- What investment options are available in my DC Plan?

- How confident am I regarding my ability to make investment decisions?
## Considerations for Plan Participants

*Capital Group:  Investments Matter*

### Sample Plan Participant
- Starting Age: 25
- Starting Annual Salary: $30,000
- Annual Salary Increase: 3%
- DC Plan Contribution: 10%

### Investment Returns
- During Working Career: 5%
- In Retirement: 4%
## Considerations for Plan Participants

### Capital Group: Retirement Age Matters

<table>
<thead>
<tr>
<th>Age</th>
<th>Ending Salary</th>
<th>Ending DC Balance</th>
<th>4% Withdrawal</th>
<th>% of Ending Salary</th>
</tr>
</thead>
<tbody>
<tr>
<td>65</td>
<td>$98,000</td>
<td>$635,000</td>
<td>$25,400</td>
<td>26%</td>
</tr>
<tr>
<td>55</td>
<td>$73,000</td>
<td>$321,000</td>
<td>$12,800</td>
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<tr>
<td>45</td>
<td>$54,000</td>
<td>$146,000</td>
<td>$5,800</td>
<td>11%</td>
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</tbody>
</table>
Considerations for Plan Sponsors

- Plan Demographics: Public Safety Only, or Broader Employee Population?

- Availability of DB Plan and/or Social Security

- Required Contributions to DB Plan
  - Aggressive DC Auto Enrollment May Not Be Ideal
Considerations for Plan Sponsors

- Customized Target Date Funds Can Better Reflect Workforce Characteristics

- Plan Should Offer a Robust Core Menu Lineup (Possibly Including Brokerage Window)

- Communication is Important

- Advice Could Be Very Valuable

- Attractive Plan Design Helps Keep Retirees In the Plan
Considerations for Investment Managers

- Develop “Mass-Customized” Public Safety Target Date Strategies
- Know Your Audience!
Thank you

Jeff Nipp, CFA, CAIA
jeff.nipp@milliman.com
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