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ASSOCIATES

# The Cerulli Report™

## Capturing and Retaining Rollovers: Positioning for Success

*Complimentary for Research Participants*

JULY 2004

### KEY FINDINGS

#### THE OPPORTUNITY

**IRAs held more than \$3 trillion at year-end 2003, with traditional IRAs comprising most of the total.** IRAs continue to represent a larger market than the defined contribution marketplace, which is now approaching its apex as the Baby Boom generation prepares to retire. Participants 50 and older now hold 59% of 401(k) assets.

**Annual rollover contributions for 2003 hit \$150 billion, a record amount that reverses three years of shrinking flows.** The surge in rollover inflows, \$19 billion more than 2002 amounts, is partly attributable to rising equity markets. It also partly reflects the lingering effects of layoffs, early retirements, and job terminations during the bear market, as many of these employees finalize their rollover provisions. The surge in contributions may also indicate ongoing success with employee education initiatives encouraging rollovers. While down from an all-time high of 71%, the ratio of rollover inflows to corporate DC distributions settled at 62% for 2003—up from 56% in 1997.

**But providers and plan sponsors remain unable to reduce the proportion of cash-out DC distributions, which has remained roughly unchanged at 20% since CA last measured it four years ago.** The inability of providers and plan sponsors to decrease the cash-out rate over the last four years suggests that they continue to face difficulties in changing participant behavior.

**Baby Boomers and job changers are fueling rollover growth, with cumulative new rollover contributions slated to exceed \$1.9 trillion between 2004 and 2010.** CA expects annual rollover inflow in 2010 will nearly triple contributions in 2003. While job changers are responsible for more rollovers, retiring Boomers are responsible for larger ones. Cerulli Associates' proprietary survey indicates that job changers account for 61% of recent rollovers—but only 46% of recent rollover assets.

**Providers still face difficulties capturing large rollover accounts, as few truly exist.** Only 19% of rollover IRAs hold more than \$75,000. This reflects the small account sizes within 401(k) plans, where the average account holds \$39,000 and the vast majority of them hold less than \$20,000; only 10% hold more than \$100,000. Some 29% of lump-sum distributions are less than \$10,000.

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## ASSET RETENTION

DC providers are only able to retain about 21% of rollover assets transferred from their 401(k) recordkeeping systems—an increase of only two percentage points over similar metrics CA measured in 1999. DC providers retained about \$32 billion of rollover assets during 2003. The consolidation that has taken place in the 401(k) market helps explain the small change in recordkeepers' rollover retention. Third-party administrator (TPA) firms presently have a greater 401(k) marketshare than they did in 1999; they also have dramatically lower asset retention rates than do competing channels. The improvements that firms implemented to tackle the rollover market during the past four years wound up blunted by the consolidation of 401(k) assets with TPAs.

**Direct-sold mutual fund companies and broker/dealers are experiencing the greatest success.** Successful asset retention rates are a direct function of the provider's efforts, both operationally and educationally, to identify and facilitate a proprietary IRA rollover option. **Broker/dealers and mutual fund companies, especially direct-sold fund vendors, are highly successful at retaining rollover assets.** Mutual fund companies only hold 44% of the 401(k) marketplace but represent 66% of retained rollover assets: US\$22 billion. Broker/dealers only represent 7% of the 401(k) arena, but hold 14% of retained rollover assets. TPAs, on the other hand, account for 5% of retained rollover assets despite their 29% marketshare of 401(k) assets.

**Advisors indicate data mining helps them ferret out rollover retention opportunities, and more concerted home-office use of such technology could not only improve rollover business but facilitate other cross-selling initiatives as well.** Respondents to a recent CA survey of bank and regional broker/dealer advisors discovered that 86% of them rely on data mining as a rollover prospecting tool. Home offices are better able to support their advisors and benefit the business as a whole if they profile the broker/dealer's overall client base. This is difficult to undertake because of the lack of technological resources and the independent nature of the advisor forces employed by many broker/dealers, but it would ultimately be beneficial for all types of firms to better understand their client base beyond the traditional account-balance and wealth-tier segmentations on which firms now rely.

**Dedicated call centers are now playing a pivotal role in asset retention. A key component of the rollover call center experience is the facilitation of rollovers to retail accounts.** CA's proprietary surveys found that 75% of providers with rollover call centers will create pre-completed rollover account applications for clients, and 50% of providers will actually contact a client's previous employer and coordinate the rollover. Almost all providers—88% of

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them-will notify clients once a rollover account has been opened. Success of the dedicated distribution/rollover center depends on the focus of the center and the compensation and incentives presented to the representatives.

**Many DC providers are increasing their spending on rollover-related training, but there is mixed consensus regarding advertising budgets.** Some 80% of DC providers are increasing their budgets in this area, according to our proprietary survey. Training ensures that frontline reps and other personnel are well versed on the intricate details surrounding retirement issues, but also includes firmwide initiatives to help employees at all levels identify client cross-selling opportunities and maximize asset retention levels. Some 82% are also increasing product-development budgets. But only 55% of respondents are spending more on advertising. Most providers agree that advertising certainly helps consumer awareness of their firm, but it does not directly generate rollover activity.

## **ADVISORS' APPROACH TO ROLLOVER**

**Nine out of ten advisors believe rollover accounts will become a larger component of their business.** Almost 56% of advisors surveyed believe that rollover assets will represent an increase of more than 16% of their client rollover assets during the next five years, and 11% of advisors expect their client rollover assets to increase by more than 40%. **But 28% of those indicate they have no plans to implement a strategy designed to increase their rollover business.** Many of these advisors are confident that rollover business will continue to come their way without requiring a tactical or strategic change in their business plans.

**Advisors responding to CA's proprietary survey indicated that on average, some 20% of their books of business already are rollover assets. Banks report the highest percentage, 23%, but the deviation among the various channels is low.** The small disparity of client assets in IRA rollovers by channel is rather surprising—because traditionally we expect to see significant client profile differences between wirehouse clients and insurance clients. CA has found that insurance advisors have the smallest average accounts. Wirehouses and RIAs, both of which have clients with much larger account balances, must attract or capture larger rollover balances in order to maintain the same proportion of rollover assets as other channels report.

**Regional broker/dealers hold a far higher proportion of DC assets than rollover accounts, while the difference between the two is slimmer in other channels.** Advisors in the regional channel said 28% of their total client assets are in DC vehicles, while only 16% are rollover assets. This obviously suggests

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that client rollovers have not been maximized. **Bank broker/dealers are the sole channel for which the proportion of client rollover assets exceeds client DC assets.** This indicates that bank advisors are most likely doing a more thorough job of client data mining and uncovering rollover opportunities.

**Advisors, especially those in the bank and regional channels, have failed to pay enough attention to securing job-changer rollover assets.** Some 67% of respondents to CA's survey classified more than 75% of their rollover clients as retirees. 33% of the advisors reported having only retiree rollover assets and only 10% of advisors reported an equal split of clients with job-changer and retiree assets. Higher-end advisors' propensity to target retirees does not mean that their clients are going through once-in-a-lifetime rollovers. In fact, 27% of advisors have rollover clients that average more than three rollovers with them, and only 36% of advisors have clients averaging only one rollover. **There are two strategies that explain why advisors have such a high percentage of retiree rollover clients: advisors are likely consolidating their clients' accounts upon retirement, or the rollovers are coming over a number of years prior to retirement.**

**Some 61% of advisors reported that their average rollover size exceeds \$125,000, making it difficult for CA to believe that advisors without access to advisory platforms will succeed in the rollover market-especially as clients consolidate rollovers as they shift jobs.** Nonadvisory-based platforms will continue to succeed in capturing the smaller balances, but even with smaller balances, they will run into problems when the accounts grow or multiple rollovers lead to higher account balances.

**Advisors actively seeking rollover assets tend to have smaller average account balances than those who do not-indicating they are more willing to look downmarket for new, younger prospects that will grow into bigger rollover clients.** Of the 40% of surveyed advisors who do not actively seek out rollover assets, 78% of them reported having average rollover account contributions of \$125,000 or more. Conversely, only 50% of larger remainder of advisors that actively seek out rollover assets reported having average client rollover contributions of \$125,000 or greater.

**Existing clients provide the majority of new rollover clients to advisors, further reinforcing the argument for increased data mining.** Current customers account for approximately 54% of new rollover accounts, almost evenly split between existing clients with new rollover accounts and existing clients transferring accounts from other rollover providers.

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## ADVICE DELIVERY AND ROLLOVER PLATFORM SOLUTIONS

Advice delivery platforms that bundle products and assistance are critical components of successful rollover retention strategies, especially for firms that lack tied advisor forces. Providers competing for IRA assets understand that a product-focused offering is not sufficient to stand above the crowd, although without the right product options a provider is not likely to even be part of the crowd. Advice and guidance is proving to be a powerful differentiator for providers trying to offer their clients plans for their retirement assets.

Lifecycle funds, advice tools, and investor centers are elements of most direct-sold mutual fund vendors' rollover platforms. Other types of DC providers so far offer less ambitious platforms, with TPAs seeking partnerships with brokers, custodians, or outsourcing vendors.

Lifecycle funds themselves are becoming a sizable component of IRA assets, with managed accounts also playing a larger role. IRA-linked lifecycle funds amounted to \$10 billion at year-end 2003, a 40% increase over 2002 levels. CA expects further growth as lifecycle options become more prevalent in rollover accounts as well. IRAs account for more than 20% of separate account consultant program assets and nearly 60% of money in mutual fund advisory programs. Respondents to our advisor survey reported that they have invested 31% of their rollover assets through managed accounts, either mutual fund advisory programs or separate account consultant programs.

More than 60% of rollover business units report to be the institutional and retail divisions of the DC provider, a strategy CA feels is effective in bridging the gap between these groups. Over the past several years, the trend is for firms to share rollover responsibilities between the institutional and retail parts of the organization, creating a unified strategy to present to all clients. A large number of DC providers also have appointed asset retention chiefs. Firms with this dedicated asset retention focus have a significant institutional presence. It is important to have dedicated individuals focusing on retaining institutional assets, but they must work closely with their institutional and retail counterparts. The participant communications, education, guidance, and advice campaigns should have a common message and theme. This unity facilitates rollover retention and creates a common experience for participants moving from an institutional platform to a retail one.