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Trends and Issues
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An analysis of white label funds in public pension plans

Introduction

White label funds are generically named funds that include one or more underlying funds. They are often named by the broad asset class the fund invests in. While white label funds are not new, they are increasingly popular options in defined contribution retirement plans. The reasons often cited by plan sponsors for adoption of these generically named funds include menu simplification, lower fund costs, and the potential to offer plan participants more sophisticated and diversified funds that can leverage the expertise of multiple fund managers. On the other hand, some requirements, like customized participant communications and increased fiduciary responsibility, present obstacles to further white label adoption by plan sponsors because they increase costs. In this study, we utilize a new database of individual-level data from public sector defined contribution retirement plans. We investigate the prevalence of white label funds in the public sector and begin to explore whether they influence participant investment allocations.

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Why should we care about white label funds?

A sizable market, growing in popularity

Over the past several years, white label funds have become more common in defined contribution menus. In 2017, Alight (formerly a part of Aon Hewitt) reported one-third of employers' defined contribution plans offered white label options (Alight Solutions 2017) up from 25% in 2014 (Hewitt Ennisknupp 2014). In terms of assets invested in these funds, Healy (2020) estimates 30% of assets in plans with more than $1 billion dollars are invested in white labels. This totals to between $750 billion and $1 trillion in assets. Larger plans are more likely to offer white label options, according to Fidelity Investments (2021). Fidelity Investments reports that 1% of Fidelity Management Trust's (FMTC) 23,000 plans under record keeping offer white labels, compared to 18% of their plans with over $1 billion in assets.

Pros and cons of white label funds

Two of the most popular reasons cited for adopting white label funds include menu simplification and the ability to incorporate multiple underlying funds into the structure, allowing plans to leverage the expertise of different fund managers. Menu simplification is possible because plan providers can decrease the number of fund options offered to participants by incorporating many different types of funds into one white labeled fund. In addition, some suggest that naming the white label fund according to the fund's investment goal can help participants better understand their investment options making it easier for them to choose. Other benefits include the ease of replacing poor-performing funds, and the potential to reduce costs to participants and plan sponsors. However, adopting white label funds may include greater operational requirements, the need for participant education, required customized communications, and increased fiduciary liabilities connected to plan sponsors. More details on white label funds can be found in Bare, Kloepfer, Lucas and Veneruso's (2017).

The influence of brands and menu effects on investment allocations

White label funds are unaffiliated with financial services brands. This is relevant because research suggests that different brand factors may influence investment choices. For example, Wang and Tsai (2014) find brand image relates to fund purchases, while Sialm and Tham (2015) find evidence that the reputation of the fund management company's brand may relate to fund flows. Agnew, Hung, Montgomery, and Thorp (2019) find in an experiment that brand trust influences whether individuals invest in a white label fund or the equivalent branded fund. This is contrary to finance theory which assumes individuals rationally choose portfolio allocations based on the risk and return characteristics of the available assets, not based on the fund brand.

Other research identifies other investment behavior related to theoretically irrelevant factors. For example, research finds that individuals' familiarity with their fund options, the fund option names, and the type and/or number of the fund options available in a menu, affect allocations (Agnew 2006; Bateman, Dobrescu, Newell, Ortmann and Thorp 2016; Benartzi and Thaler 2001; Brown, Liang and Weisbenner 2007; Cohen 2009; Cooper, Gulen and Rau 2005; Green and Jame 2013; Huberman 2001; Huberman and Jiang 2006; Tang, Mitchell, Mottola and Utkus 2010).[1] Taken together, the evidence suggests that plan sponsors should consider the potential unintended consequences of altering fund menus before they change plan menus. This research also suggests that the introduction of white label funds into defined contribution plan menus could affect investor behavior. Thus, these findings motivate our current study.

White labels and the public sector defined contribution market

Given the limited information related to white label use in practice, this paper significantly contributes to our general understanding of white label funds in the public sector market. Until recently, researchers interested in white label funds were limited to studying hard-to-access proprietary administrative data or conducting their own surveys. While researchers interested in plan menus often turn to public data from annual filings of Form 5500, this form does not require information related to white label assets (Healy 2020). It is not until recently that participant-level data on white label offerings became available through the 2020 release of the Public Retirement Research Lab (PRRL) Database (https://www.prrl.org/).

1 Agnew, Hung, Montgomery, and Thorp (2019) provide a brief overview of these studies.

Why are defined contribution plans in the public sector interesting?

Most retirement research focuses on retirement plans in the private sector, but public sector retirement plans are arguably more interesting to study because their employees face relatively more complicated choices. In the public sector, most full-time state and local government employees are typically covered by a defined benefit retirement plan. Generally, public employees are required to participate in that plan. However, employees are also often offered one or more supplemental defined contribution retirement plans. For example, state and local governments are allowed to offer both 401(k) plans and 457(b) plans to employees.[2] In addition, public schools, hospitals, and charitable organizations can also offer 403(b) plans. Finally, 401(a) plans are available to government agencies, educational institutions, and non-profit organizations.[3] These plans tend to be voluntary. As a result, some public employees not only have to decide whether to save in a supplemental defined contribution plan, but also, in many cases, they must choose which plan or combination of plans to contribute their savings to each year. In some cases, participants are choosing from two to four plans. These are decisions that some participants in the PRRL data face. In this study, data on 401(a), 401(k) and 457(b) plans are available. Clark, Pathak and Pelletier (2018) provide an informative overview of the complex supplemental public defined contribution market for those looking for more details.

Overview of the Public Retirement Research Lab (PRRL) Database

The Employer Benefit Research Institute (EBRI) and the National Association of Government Defined Contribution Administrators (NAGDCA) created the Public Retirement Research Lab (PRRL) Database (https://www.prrl.org/). Plan sponsors voluntarily join the Public Retirement Research Lab and their recordkeepers transmit de-identified participant-level data on their plans' behalf. These data include individual asset allocations based on contributions and balances. Another distinguishing feature of the PRRL database is that it includes some demographic data. While not available for all plans, most of the PRRL participant-level data includes gender (95%) and age data (almost 100%). Data on job tenure (68%) and salary (44%) are more limited. These data collected from multiple public plan sponsors through their recordkeepers provide the most comprehensive participant-level information related to the public sector defined contribution industry available for public research.

Table 1 provides a broad overview of the data in the 2020 PRRL. The PRRL 2020 database includes 212 plans, but we restrict the sample to 207 plans that fall into the data's three main plan types (401(a), 401(k) and 457(b)). Table 1 presents summary statistics for all plans and by plan type. In total, plan assets account for $112 billion dollars and 2.3 million accounts. Table 1 also breaks the plans down into the category of employee types covered by the plans. Plans often include participants representing more than one category of employees. As a result, the total number of plans for each plan type is less than the sum of the plans covering each category of employee.

2 Note while public employers can offer 401(k) plans, federal legislation passed in 1986 restricted employers from creating new 401(k) plans after its enactment. As a result, existing 401(k) public plans predate 1986 (Clark, Pathak and Pelletier 2018).

3 401(a) plans, and public sector retirement plans more generally, do not fit neatly into the dichotomy of an employer-sponsored pension or individual-based retirement account. For example, some 401(a) plans are mandatory for employees to participate in as part of a "hybrid" DB-DC retirement system. See "What are Hybrid Retirement Plans, A Quick-Reference Guide" (NASRA, https://www.nasra.org/Files/Topical%20Reports/Hybrids/Hybrid-primer.pdf) for additional details.

This table summarizes the plans included in the PRRL database by their plan type (401(a), 401(k) or 457(b)). For each type, the aggregate plan assets, number of participant accounts, and category of employees the plan covers (for example, state or city employees) are tabulated. Plans often include more than one category of employees. Therefore, the total number of plans for each plan type is not equal to the sum of the plans covering each employee category.

Table 1. Summary of 2020 PRRL database

	401(a)	401(k)	457(b)	All
Number of Plans	68	14	125	207
Plan Assets	$32,831,858,217	$26,997,363,541	$52,548,938,840	$112,378,160,599
Number of Participant Accounts	789,747	567,494	943,522	2,300,763
Number of Plans Serving				
State Employees	19	8	23	50
City Employees	37	9	73	119
Hospital Employees	4	4	13	21
School Employees	4	7	14	25
County Employees	21	5	32	58
Special District Employees	13	5	13	31
College Employees	5	6	15	26
Other Employees	15	0	19	34

Key insights into the public sector market and white label fund options

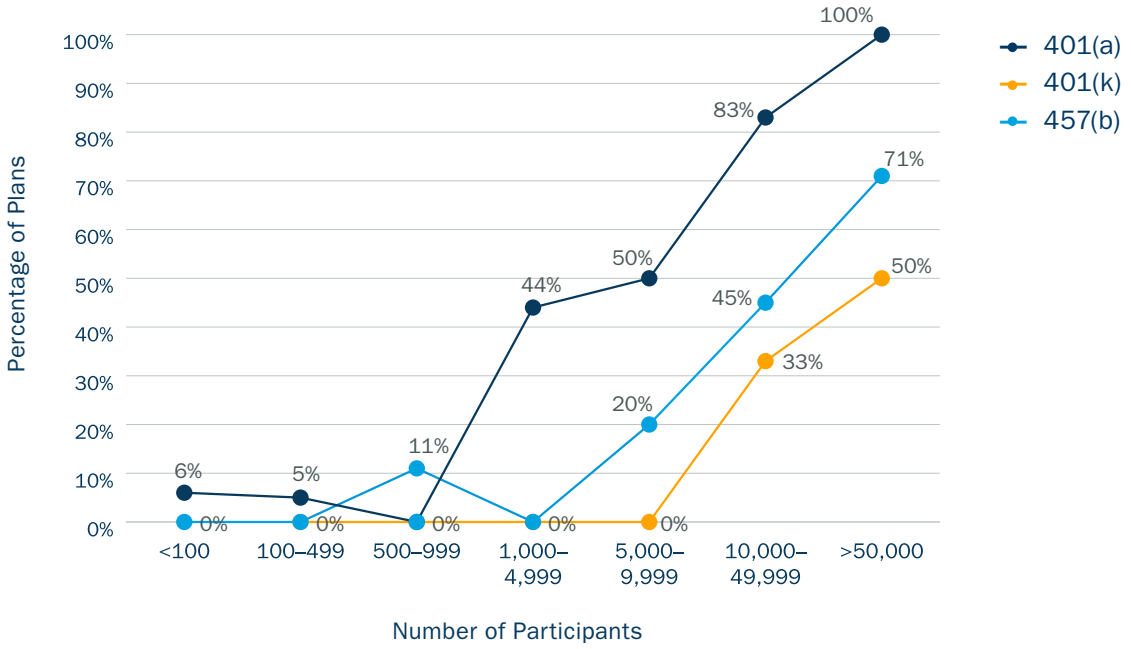
As discussed earlier, public sector employees are often offered multiple defined contribution plans to join. Thus, one person may represent multiple accounts in the PRRL database. For our plan-level analysis, we focus on 'participant accounts' not unique participants. However, we use unique participants in our participant-level analysis, choosing the plan in which the individual holds the largest balance.

We also break down plan menus into four types: 1) all branded, 2) mixed menu, 3) only stable value white labeled, and 4) white label only. All branded menus have no white label options. Mixed menus include white label and branded options. Only stable value white label menus are a special case where all the fund options are branded except for the white label funds. We do not consider this special case a white labeled menu, but others might. White label only fund menus include only white label options but may also include a self-directed brokerage option. A plan offering a white label option, according to our definition, includes plans with either white label only menus or mixed menus.

- **A significant number of participant accounts reside in plans offering white label funds.** Sixty-six percent of participant accounts are in plans offering white labels as a fund option. These numbers vary with plan type; 91% of participant accounts in 401(a) plans, 51% of participant accounts in 401(k) plans, and 54% of participant accounts in 457(b) plans are in plans offering white label funds.
- **Larger funds are more likely to offer white label fund options**. Prior research suggests that implementation costs might make it more expensive for smaller plans versus larger plans to offer white label options. Consistent with this, our results show that the percentage of plans offering white label funds increases with the number of participants enrolled in the plan. Figure 1 shows this trend.

Figure 1. Percentage of plans with white label funds by plan size

This figure displays the percentage of plans with white label fund options by plan size measured by participants enrolled in the plan.

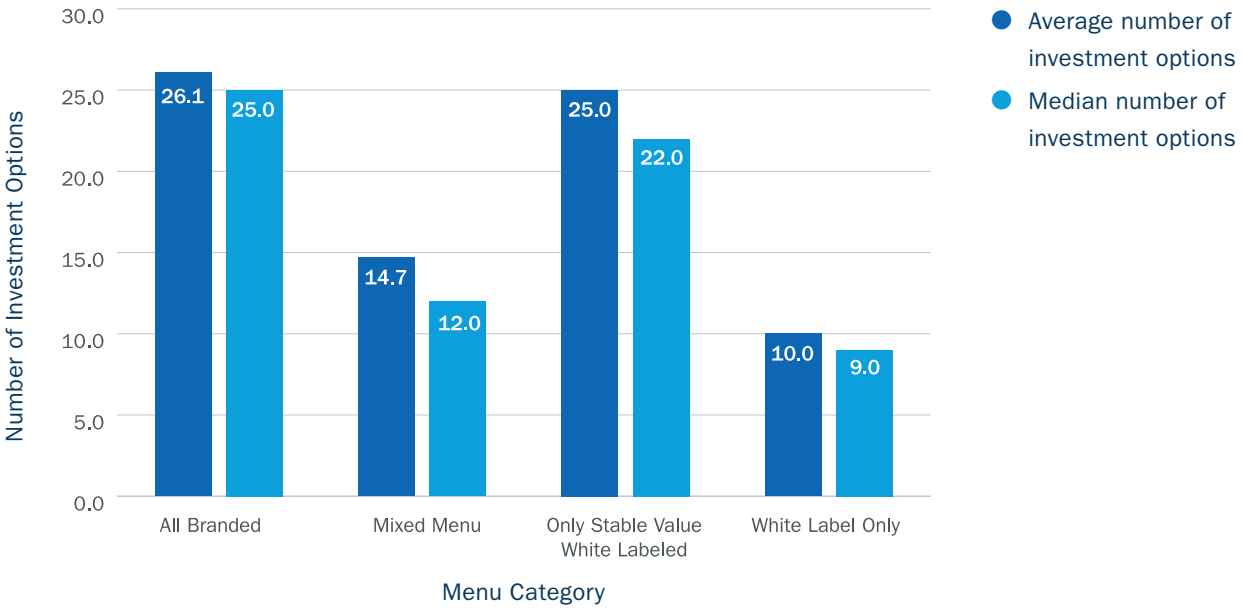


- **Mixed menu plans are not uncommon.** Mixed menus include both branded and white label funds.[4] While the 401(k) plans in the database offer only white label only menus, mixed menus represent approximately 40% of 401(a) and 457(b) plans in the data. Given the possible branding effects, these are an interesting subset of plans for future research.
- **White label only and mixed menus appear to offer simpler menus.** Figure 2 supports the assertion that white label funds simplify plan menus. The figure shows white label only menus and mixed menus have the lowest average number of investment options (10.0 options and 14.7 options) versus all branded menus (26.1 options). In terms of options offered, we find our special category of branded menus with white labeled stable value options (25 options) is most consistent with all branded menus (26.1 options). We find similar results based on fund families represented in the menu. However, the white label and mixed menus still offer a similar broad selection of asset classes relative to branded menus.

4 We cannot determine from the data if all the employees in the plan have access to all the funds. We can imagine a scenario where a plan is changing its menu and offers new employees a more limited menu of the new funds than current employees. We do not know the specific plans included in the PRRL database, but we have confirmed through internet searches of public plan information that several plans exist that offer mixed menus to all participants (new and old hires combined).org/Files/Topical%20Reports/Hybrids/Hybrid-primer.pdf) for additional details.

Figure 2. Average and median investment options

This figure displays the average and median number of investment options offered based on menu type.



- **Our participant-level analysis finds preliminary evidence that white label** funds are associated with greater use of self-directed brokerage windows albeit to a very small degree. Therefore, it is not clear from our results whether this is cause for concern. We view our early findings as motivation for further research.

Conclusions

White label funds are becoming increasingly popular. Still not much is known about how these funds are integrated into defined contribution menus. To address this, our paper takes advantage of a new database that includes both plan and participant-level data related to public sector plans.

At the plan level, we find that white label funds are more prevalent in larger plans and surmise that it is due to the implementation costs. White label only and mixed menus appear more simplified as they tend to offer fewer fund options and fund families relative to branded menus. Mixed menus that include brand and white labels are not uncommon.

At the participant level, we find preliminary evidence that white label funds are associated with greater use of self-directed brokerage windows albeit to a small degree. Therefore, it is not clear from our results whether this is cause for concern.

In closing, we hope our plan level analysis serves as a useful guide to plan sponsors interested in how different plans incorporate white label funds into their menus and suggest that our early participant level findings serve as motivation for further research.

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