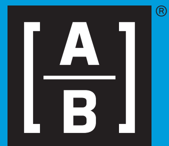


INSIDE THE MINDS OF PLAN SPONSORS

MOVING TO THE FUTURE OF DEFINED CONTRIBUTION PLANS

IN THIS PAPER: Having conducted over a decade of plan sponsor and participant research, we've charted the evolution of defined contribution (DC) plans—how the government, retirement industry and plan sponsors have enhanced retirement readiness for American workers. In this latest installment of our survey research, we're seeing some helpful trends becoming the accepted standard, including automatic enrollment, automatic escalation, and the widespread use of qualified default investment alternatives (QDIAs) such as target-date funds. But there are also new frontiers that can further improve retirement readiness, as well as some problematic trends that need attention and change.

ABOUT AB'S DEFINED CONTRIBUTION RESEARCH

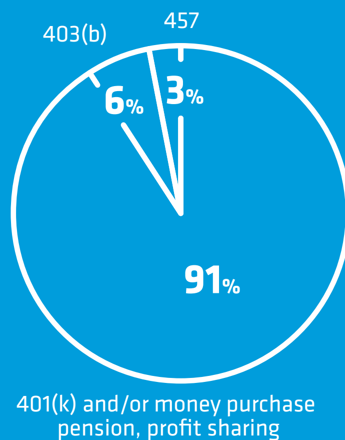
In late 2016, AB's defined contribution team conducted a web-based survey of over 1,000 DC plan sponsors. The survey's respondents had roughly equal representation from all plan sizes across the full universe of DC plans. So, the survey doesn't necessarily reflect the status quo for overall DC assets, which are more heavily weighted to the largest plans (referred to here as "institutional" plans).

Here is the breakdown of respondents by plan size:

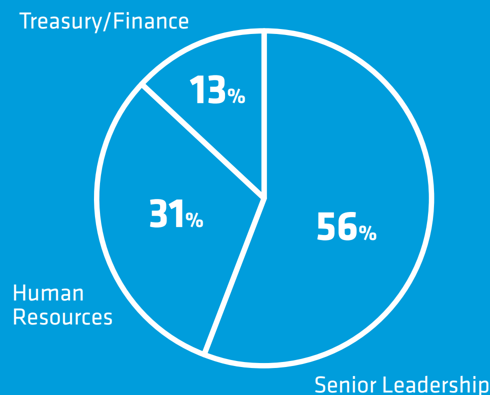
Segment	Plan Size	Number of Respondents
Micro	<$1 Mil.	202
Small	$1 Mil.–$9.9 Mil.	209
Mid	$10 Mil.–$49.9 Mil.	194
Large	$50 Mil.–$249.9 Mil.	196
Institutional	$250 Mil.–$500 Mil.	95
	>$500 Mil.	104

The goal was to understand how plan sponsors feel about the current state of their companies' plans, their participants and the DC industry. This publication includes the key findings from our survey. It comprehensively updates the research we last conducted in 2014.

ORGANIZATION TYPE (% OF TOTAL)
9 in 10 organizations have 401(k) plans



RESPONDENT ROLE IN ORGANIZATION (% OF TOTAL)*



* Role definitions: "Senior leadership" is a chairman, president, CEO, business owner, executive director or other senior management positios; "Human resources" is a human resource or employee benefits position; "Treasury/Finance" is a CFO, chief investment officer, or other financial, investment or treasury position. Due to rounding, numbers may not sum to 100%.

OVERVIEW

Defined contribution (DC) plans hold the key to solving the retirement readiness dilemma for American workers. To varying degrees, plan sponsors recognize the need to take a more comprehensive approach in preparing today's workers for tomorrow's financial well-being.

Coming to grips with an aging workforce. Should companies encourage retiring employees to keep their assets in the plan? With the US Department of Labor (DOL) increasing its scrutiny of IRA sales, it's a good time for companies to develop an organizational policy.

+ Only half of plan sponsors track participant cash-out activity (versus rollovers to an IRA or other qualified plan).
+ Roughly half have no stated preference concerning cash-outs.

Financial wellness programs viewed as a smart investment. Plan sponsors using these programs see higher levels of employee engagement and productivity at work as well as improved perceptions of their organization.

+ Financial wellness programs are sorely needed: 90% of surveyed workers can't correctly answer eight simple questions about investing.[1]

Fiduciary awareness is slipping. More than half of plan sponsors don't realize they are fiduciaries.

+ Sponsors who use a financial advisor or consultant have a better understanding and awareness of their fiduciary responsibilities than those who don't use an advisor or consultant.

Good news: Savings are up. Roughly half of plans report an increase in participation rates and deferral rates over the past three years—an encouraging sign of progress.

Bad news: We have a long way to go. The majority of plan sponsors worry that their participants don't know how much they need to save and won't save enough to retire.

Great news: Reenrollments are "on the menu." More plan sponsors see that reenrollments boost participation rates, deferral rates, diversification—and retirement readiness.

+ In 2013, only 10% of our respondents said they were considering a reenrollment in the near future.
+ But since then, over 40% of respondents in this survey say they have recently done a reenrollment, and 23% say they're considering it in the next two years.

Target-date funds continue to innovate and lead as QDIA of choice. But some plan sponsors may not be aware of cost-saving target-date innovations available for their plans.

Automatic escalation continues to grow. While adoption of automatic enrollment may be levelling out, adoption of automatic escalation is rising—and often, at a higher pace than 1% of salary per year.

+ More small plans are using auto-escalation than in the past, but larger plans still lead in this regard.

1 AB, *Inside the Minds of Plan Participants*, March, 2017.

REDEFINING CONTRIBUTIONS TO EMPLOYEE BENEFITS

In 2000, about 12% of the US population was over 65. By 2050, it will be nearly 21%. Few American workers or companies are prepared. But DC plans have started incorporating innovative tools to help the workforce…and the workplace.

AGING WORKFORCE CALLS FOR NEW RESPONSES

Along with the march of baby boomers into retirement, there's a shift in the mindset of many workers about when to retire. Currently, the average retirement age in the US is 63.[2] But retirement savings for most workers are low, more defined benefit (DB) plans are being frozen or eliminated, and full Social Security benefits aren't kicking in until age 66 (and going up to 67 for those born after 1960). The result: employees are increasingly working longer.

More than half our respondents (56%) say the average retirement age at their company has risen over the past five years. They also expect that nearly one-fourth of employees (23%) will hold off on retiring until after age 67.

These trends are putting increasing pressure on DC plans with regard to how involved plan sponsors should be in participants' DC account decisions when they retire.

When plan sponsors are asked about their organization's philosophy regarding terminated or retired participants' balances in the plan, the most common response (37%) is that participants should roll over their assets into an IRA or another qualified plan. The next most-cited response (28%) is that their company has no philosophy one way or another. But 18% feel participants should keep their money in the plan. Only 7% see taking a lump-sum distribution (a cash-out) as the answer, while another 7% feel participants should buy an annuity.

While most plan sponsors don't think a cash-out is a good idea, there's no consensus on how to approach the issue with employees. Only half of our respondents' organizations even track the percentage of participants who cash out. And nearly as many (48%) feel that cash-outs are none of their business—the money belongs to the employees, and they can do whatever they want with it.

But we're seeing a growing paternalistic concern: 23% of plan sponsors say they'd rather participants put the assets in another qualified account, and nearly as many (21%) would prefer that participants leave the money in the plan, because the plan will be able to negotiate better fees by virtue of higher balances.

Interestingly, 14% of plan sponsors feel cash-outs are "a waste of the money we contributed to the plan." That's a bit harsh, considering that company match contributions are competitive table stakes for hiring and retaining employees, not simply a generous addition.

There are pros and cons on whether or not to encourage employees to keep assets in the plan. After all, plan sponsors face continued fiduciary liability and administration for those assets. However, by keeping assets intact, plans may well be able to access better pricing. And that's not simply a selfish concern on the part of plan sponsors! A paternalistic attitude could save their employees from higher fees they may get charged in other investing vehicles. Also, lump-sum cash distributions turn too many people into "kids in a candy store."

FINANCIAL WELLNESS PROGRAMS: SURPRISING PAYOFF FOR AN INNOVATIVE EXERCISE

Retirement unreadiness is such a pressing issue for American workers that it needs to be attacked from any and every angle possible. So it's heartening to see the positive early results for financial wellness programs, often broadly defined by topics like budgeting, paying for college, and financing a home. As with many innovations for DC plans, the early adopters of financial wellness programs are more concentrated in larger plans, with half of institutional-size plans already participating. Only one-fourth of micro and small plans are taking part.

Companies offer these formalized, needs-driven programs to employees as additional resources, separate from the 401(k) education program. According to our survey respondents, the most common services are investment planning (53%), targeted education programs (51%) and seminars (48%).

While financial wellness programs have only begun to gain popularity as formal programs, already four in ten (38%) plans offer them. And the median participation rate of roughly 30% is surprisingly robust, considering they're entirely optional and not directly related to employee benefits, such as the DC plan.

2 US Census Bureau

Source: AB Research, 2016

Plan sponsors whose companies offer these programs frequently cite several important benefits. More than half (51%) say employees are more engaged, and nearly as many (47%) say employees have a better perception of the organization. But two other metrics are even more noteworthy: four in 10 plan sponsors report that employees are more productive and focused, and one-third say employees are less stressed.

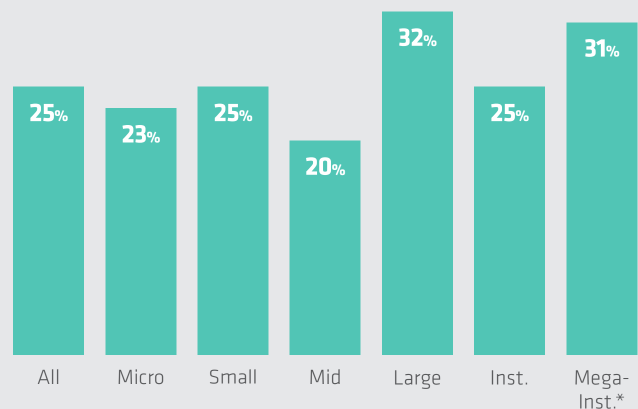
These responses certainly indicate a win-win from financial wellness programs. Companies have more engaged, productive employees who've improved their financial knowledge and confidence—and those employees will more likely be able to retire when they want. Of course, it's still a bit early to know if workers' retirement readiness and savings have actually improved, but these financial wellness programs seem to help steer them to better savings decisions.

REBOOTING WITH ROBO-ADVICE

Another DC participant-servicing tool is robo-advisor services. While they've been around for years, there has recently been an explosion of new providers, and these digital investment advice tools have evolved into a wide spectrum of variations on the theme of using automated techniques to build and manage portfolios. Typically based on computer algorithms, robo-advice for DC plans can provide a low-cost level of interactivity for individual participants, regardless of their account balances. Robo-advice could also be cost-effective to plans by potentially lowering call-center use.

As with financial wellness programs, larger plans have taken the lead—roughly 40% of institutional-size plans versus less than 20% of small and micro plans. And like plans using wellness programs, those offering robo-advice services are more likely to have noted an increase in plan participation over the last three years: 58% versus 43% of plans without robo-advice.

Overall, more than one-fourth of plans (27%) offer robo-advice to their participants. And roughly 25% of participants in these plans access the robo-advice service. In addition, about one-fourth of our respondents who don't currently use robo-advice now say they either are considering it or aren't sure at the moment



* Mega-institutional plans are those of >$500 million.
Source: AB Research, 2016

FIDUCIARY ROLE/RULE: TIME TO UPGRADE AWARENESS

The new fiduciary rule from the DOL primarily affects financial advisors. But DC plan sponsors—longstanding fiduciaries under ERISA rules[3]—also face added responsibilities. Because of legal ramifications, what you don't know can truly hurt you.

NEW RULES: MORE CARE AND PRUDENCE

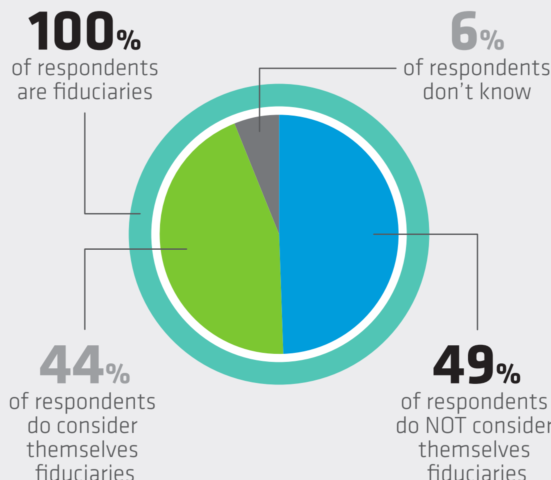
Although the DOL delayed implementation of its landmark fiduciary rule to June 2017, the implementation horse was already out of the barn. The fiduciary status of retirement plan sponsors has been a fixture for decades, and that stays the same. But their interactions with advisors, consultants and recordkeepers now have added considerations.

Some service providers who weren't previously considered fiduciaries will now fall under that designation, even if their services haven't changed. And many issues of fee structures, co-fiduciary liability, and investment advice or recommendations given to an employee benefit plan will require closer investigation, understanding and vetting by plan sponsors.

For example, robo-advice has been blessed by the DOL, but plan sponsors still have to make sure they understand what a particular robo-advice service is doing, what the algorithm entails, and how the associated fees to the plan and to participants are calculated.

That added scrutiny is unlikely to take place if plan sponsors don't even know they're fiduciaries—legally responsible for acting solely in the interest of plan participants with the care and prudence of a person knowledgeable in this field.

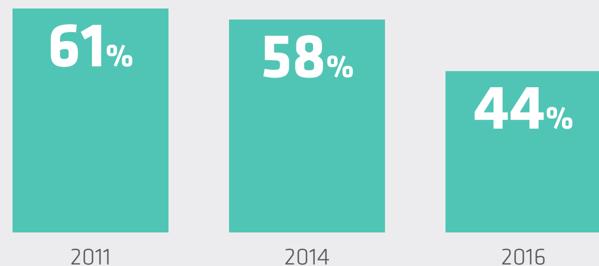
DO YOU CONSIDER YOURSELF, PERSONALLY, A PLAN FIDUCIARY?



Due to rounding, numbers may not sum to 100%.
Source: AB Research, 2016

DECLINING SELF-PERCEPTION OF WHO IS A PLAN FIDUCIARY

Plan sponsors who consider themselves, personally, plan fiduciaries.
% of respondents



Source: AB Research, 2016

ARE YOU A FIDUCIARY? (HINT: THE ANSWER IS YES!)

Sad to say, plan sponsors have never scored highly on knowing their fiduciary status. (By the way, all of our respondents qualify as fiduciaries based on their role in the plan.) But that awareness has deteriorated significantly in recent years. In fact, those who know they're fiduciaries are now in the minority. And while the survey allowed a "don't know/not sure" response, no one should be guessing about their fiduciary status.

Curiously, when asked how confident plan sponsors are that all fiduciaries for their plan understand each of the six core standards of conduct required of fiduciaries (see Appendix, page 16), over 70% say they're confident or very confident for each core standard. That's a big gap.

FOR FIDUCIARIES, THERE'S AN "I" IN "TEAM"

There could be any number of reasons why we're seeing this continuing decline, but the survey details can provide some targeted solutions.

Of the four plan designations that qualify as fiduciaries, the two categories that denote individual responsibility are generally more aware of their status. Roughly two-thirds of those with primary responsibility for the plan know they're fiduciaries, and over half of those who say they make all decisions associated with the plan know their status.

But fiduciary awareness drops significantly in the two team categories—investment or administrative committees. With that in mind, one quick fix would be to remind all team members that they are both individually and collectively responsible as fiduciaries for the plan.

3 The Employee Retirement Income Security Act of 1974 (ERISA) is a federal law that sets minimum standards for most voluntarily established pension and health plans in private industry to provide protection for individuals in these plans.

Clearly, fiduciary training could help bring awareness more in line, and about two-thirds of plans offer fiduciary training programs. While that's encouraging, about half the respondents who have access to a training program don't think it's comprehensive. And while 80% of respondents say their plans document the fiduciary process, more than half of them feel the process could be improved.

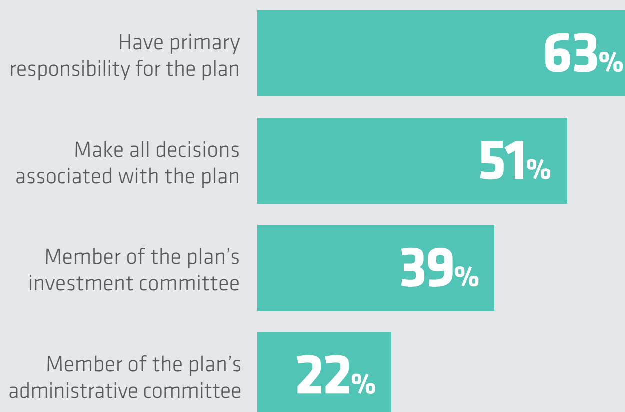
TIME TO VALUE FIDUCIARY AWARENESS

When sponsors are asked to rank the most useful components of services provided by recordkeepers and advisors, fiduciary responsibility reviews are near the bottom of the list, below investment monitoring and reviews, employee investment education, customer service for sponsor and participants, and plan fee reviews. It appears fiduciary responsibility is underappreciated, but that's mostly apparent among those who don't know they're fiduciaries—only 16% find fiduciary review extremely useful versus 24% of plan sponsors who recognize their fiduciary status.

FINANCIAL ADVISORS/CONSULTANTS CAN HELP

One way to boost fiduciary awareness and appreciation is to hire a financial advisor or consultant. Many larger plans typically have access to in-house resources, but that's less likely (and sometimes a bit costly) for smaller plans.[4] Even with these smaller plans, two-thirds of plan sponsors (65%) do use a financial advisor or consultant.

THOSE WHO KNOW THEY ARE FIDUCIARIES—PERCEPTION OF RESPONSIBILITY BY ROLE IN THE PLAN



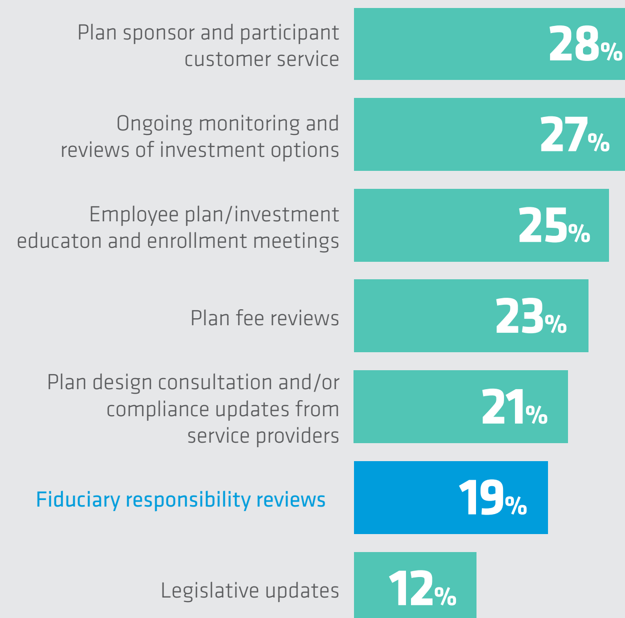
Source: AB Research, 2016

Why? Most respondents (59%) say that they want to have an objective check on the advice they get from their plan's other service providers. And the services they most frequently use financial advisors/consultants for are providing investment advice as a fiduciary (58%) and plan documentation/due diligence services (57%).

Using others for these critical services may be part of the reason some plan sponsors feel they're not on the hook as fiduciaries. But beware: it's more likely that both you and the financial advisor/consultant are co-fiduciaries, and you could still be liable for a breach of fiduciary responsibility by "another fiduciary." That's just one more reason to have all your plan sponsors brush up on their fiduciary responsibilities.

And it's likely that your plan sponsor colleagues want to do just that. Nearly half of our total survey respondents (48%) feel the DOL's new fiduciary rule is definitely necessary, and another 41% say it's somewhat necessary. Very few (11%) feel it's not really needed.

HOW USEFUL ARE EACH OF THESE SERVICES TO YOU?
Percentage of respondents who find service extremely useful



Source: AB Research, 2016

4 Our survey asked plans with less than $50 million in assets.

TRENDS AND INNOVATIONS IN TARGET-DATE FUNDS

With each passing year, not only are more plans using target-date funds, but there are more reasons to use them—and more styles of target-date funds to fit almost any plan's needs.

STEADY INCREASE AMONG ALL PLAN SIZES

Use of target-date funds continues to grow. The increase from our last survey is most notable among micro plans, because they clocked in at a rather low 33% in 2014. So an increase to 40% in this survey is quite a big jump.

Our survey's results for large and institutional plans seem somewhat low when compared with those from industry surveys.[5] But our survey also reported rather sizable percentages of respondents who say they're planning on adding target-date funds—at least 20% across all plan sizes. And the number of sponsors from large and institutional plans who say they are not adding target-date funds more closely corresponds with industry tallies of these large plans.

Over the past decade, a wide array of target-date funds have come to market, adding to the first generation of prepackaged proprietary mutual fund vehicles that typically came with that company's recordkeeping services. While many DC plans are still using those target-date 1.0 versions, today there are many more options. These include nonproprietary, multi-manager mutual fund offerings as well as customized target-date solutions and solutions that use collective investment trusts (instead of mutual funds) as the underlying vehicle.

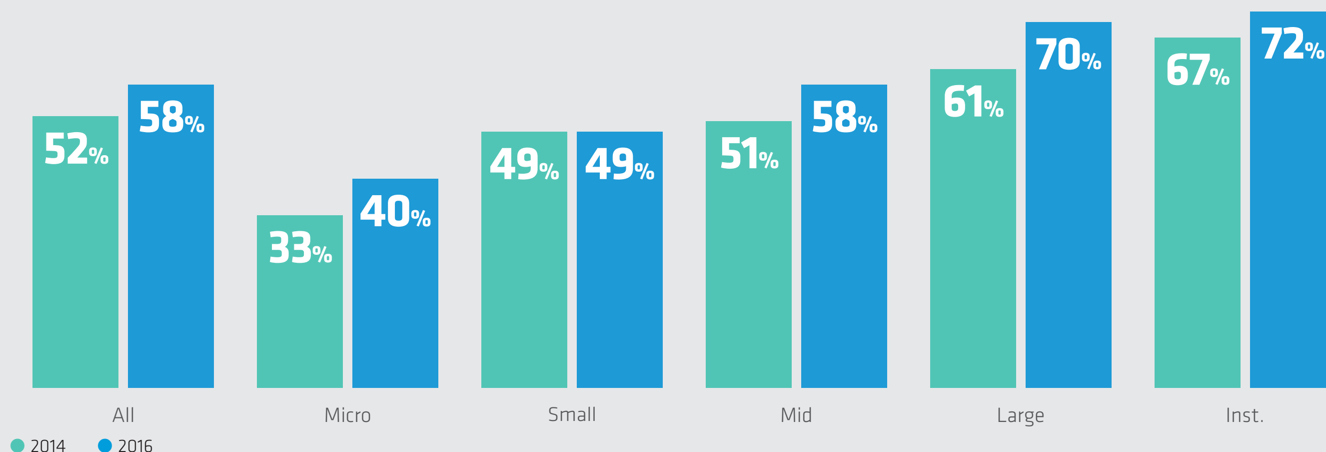
ASSESSING TARGET-DATE FUND PERFORMANCE

Whichever target-date solution companies use, our respondents point to performance first when asked what they think are the most important attributes. Next, they mention cost, quality of asset management and having an appropriate glide path.

While investment performance is still the top attribute when assessing target-date funds, it's less important now than it was in our 2014 survey, when it was cited by 65%. Perhaps, this reflects the greater distance from the crisis of 2008–2009, and the slow but steady rebound of both the economy and equity markets. It may also reflect the greater spectrum of target-date fund asset classes for diversification—as well as overlays that can reduce some of volatility's damage.

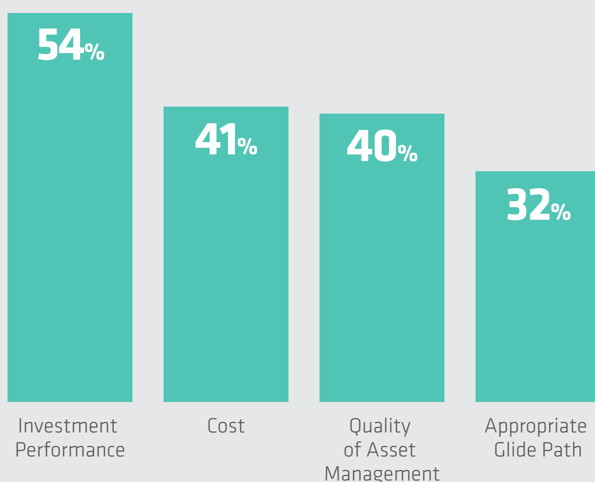
MORE PLANS THAN EVER ARE OFFERING TARGET-DATE FUNDS

Do you offer a target-date fund? (% of respondents)



Source: AB Research, 2016

5 Callan Associates reports that nearly 93% of large plans it surveys have a target-date fund in their lineup.



Source: AB Research, 2016

EQUAL IMPORTANCE PLACED ON COST AND QUALITY

Cost ranks second among issues that plan sponsors assess when looking at target-date funds. But interestingly, it's essentially just as important as concerns about the quality of asset management. That brings up the issue of balancing fees with providing an effective menu of investment options, including the choice of target-date solution.

One line of thinking says investing in funds with the lowest fees will ensure compliance with fiduciary responsibilities. But low fees aren't a panacea for the many fiduciary considerations plan sponsors have to address. It's fair to say that if a plan sponsor chooses a plan investment solely because it's the lowest-fee option, that plan sponsor hasn't engaged in a prudent fiduciary process.

The DOL's fiduciary duty guidance with regard to fees is that plan sponsors should ensure fees are reasonable, not simply the lowest. Certainly, plan sponsors are keenly aware of potential litigation over excessive fees. But "not the lowest" is not the same as "excessive." One risk of focusing too much on fees is creating a distortion that addresses cost while possibly overlooking other retirement-saving factors. And many plan sponsors are on shaky ground when it comes to understanding fees: only 54% of our respondents say they are confident or very confident that they understand all of the fees their plan is paying.

IF YOU'RE CONCERNED ABOUT FEES, CONSIDER CITS[6]

Our survey results indicate that too many plans—of all sizes—aren't taking advantage of some target-date enhancements and cost-saving variations on the market today. Roughly 40% of plans still use first-generation off-the-shelf proprietary mutual funds. And with fees coming under greater scrutiny each year, we feel that more plans could find cost savings by using collective investment trusts (CITs) as the underlying vehicles for both stand-alone menu options and the investment sleeves in target-date funds.

While CITs have been around for 60 years, they've been enhanced recently. Now, they offer most of the convenience of mutual funds, but with lower fees and flexible pricing. Industry research shows that CIT use in target-date funds is growing rapidly—from 19% use in 2012 to 39% in 2016, only four years later.[7] And CITs could grow to more than 28% of total DC assets by 2025—nearly $3 trillion in total assets. They've become gradually more accessible for smaller plans as minimum asset requirements have been lowered by many asset managers.

6 The Units within a CIT are securities which have not been registered under the 1933 Act and exempted from investment company registration under the Investment Act of 1940. Therefore, Participating Plans and their Participants will not be entitled to the protections under these Acts.

7 Morningstar Direct, Strategic Insight Simfund and AB Research

INTO THE FUTURE: GUARANTEED LIFETIME INCOME

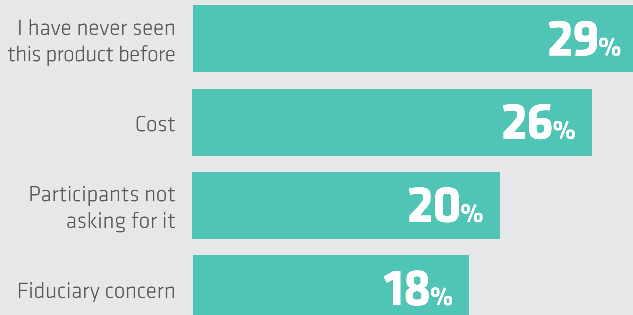
A more profound target-date enhancement is starting to get noticed: incorporating a guaranteed income stream for life.

We asked sponsors of plans with $10 million or more in assets about this type of fund, and 68% say it is appealing or extremely appealing. But such funds are quite new, and nearly one-third of sponsors who find it appealing say they haven't yet added it as a plan option, because they haven't seen it before. Another 26% feel that costs will be a hurdle, and some see the potential for fiduciary concerns or legal risks, and want regulatory and safe harbor clarity from the DOL first. The DOL has made some movements lately in favor of using these options in plans, and we're hoping to see more specific guidance in the near future.

Some respondents in our plan sponsor survey are concerned that their participants won't want this type of target-date fund with a guaranteed lifetime income component. But in our recent survey of plan participants, 84% of current target-date fund users find such a fund to be appealing or extremely appealing, and even 65% of nonusers agree. Also, 62% of nonparticipants say they'd be interested in such a guaranteed-income target-date fund—and that it would enhance their desire to participate in the DC plan.

YOU MENTIONED THAT YOU FIND THIS GUARANTEED LIFETIME INCOME APPEALING. WHY HAVEN'T YOU ADDED THIS OPTION TO YOUR PLAN?

% of respondents in mid-large market who found appealing



Source: AB Research, 2016

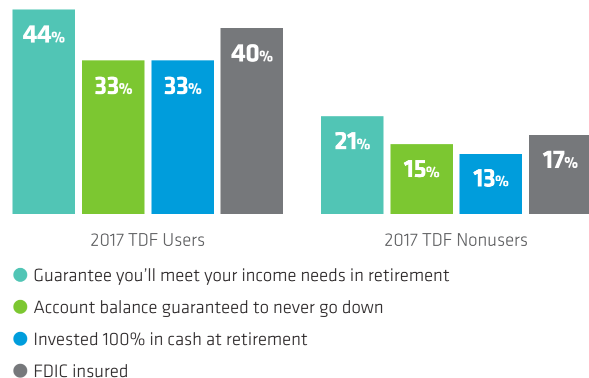
DO PARTICIPANTS REALLY UNDERSTAND TARGET-DATE FUNDS?

In our surveys of plan participants, we've seen a decline in how much workers understand about target-date funds—even among target-date fund users. Perhaps that's tied to more participants being automatically enrolled in target-date funds (their plan's QDIA), so they don't feel a need to investigate and learn the mechanics of target-date funds.

Beyond understanding these funds' mechanics, plan sponsors feel that only half their participants use them properly (i.e., investing 80% or more of their assets in one target-date fund).

MISINFORMATION PLAGUES TARGET-DATE FUNDS

Respondents answering incorrectly



Source: AB, *Inside the Minds of Plan Participants*, March, 2017

AUTOMATIC FEATURES GENERATE RESULTS—FOR PLANS AND PARTICIPANTS

While usage of automatic escalation continues to rise, automatic enrollment seems to have reached a plateau. It's eye-opening to look at some plan metrics that make a compelling case for auto features.

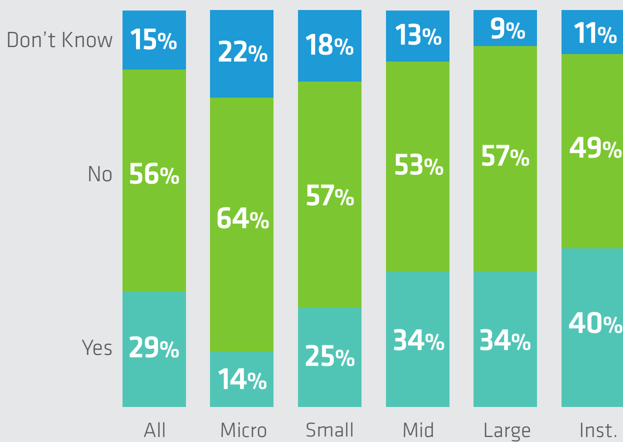
AUTOMATIC ENROLLMENT LEVELS OFF

Across all plan sizes, the adoption of automatic enrollment of workers into the company's DC plan remains at 55%, the same as in our 2014 survey. But the 2016 survey had a slight uptick among respondents who say they don't know or aren't sure if the plan uses automatic enrollment. And despite the static average number, it's worth noting that the average percentage for plans with $50 million or more in assets is notably higher, roughly 69%.

It will be interesting to see if these percentages increase in future surveys. It has taken the economy—especially the job market—a long time to trend positively enough to make business leaders more confident in planning for future business growth. As more companies go from "wait and see" to "time to grow," there may be a new surge in improving overall benefits packages to entice the best possible candidates in a much tighter job market.

LARGER PLANS ARE MORE LIKELY TO AUTOMATICALLY ESCALATE

Use of automatic escalation by asset size (% of respondents)



Source: AB Research, 2016

RIDING THE AUTO-ESCALATOR

Automatic escalation of participants' contribution rates is typically the next step beyond auto-enrollment. Fewer plans have adopted auto-escalation, but its use continues to grow. The average across all plans stands at 29%, slightly higher than the 26% reported in 2014. And this number, too, might be skewing lower owing to a rise in survey respondents who say they don't know or aren't sure if they use auto-escalation (from 7% in 2014 to 15% in 2016).

As with most innovations in DC plans, larger plans have taken the lead with auto-escalation. For plans over $50 million in assets, 37% use this feature. Some plan sponsors may be reluctant to use automatic escalation because it might feel too invasive in the decision-making process for these participant-driven retirement savings plans.

Despite appearing to be a step too far for some plan sponsors, it's worth noting that auto-escalation doesn't trigger much more of an opt-out rate than auto-enrollment. One in five employees (20%) opts out of auto-escalation, compared to 12% for auto-enrollment. Both are good examples of successfully using inertia for the benefit of employees.

ONLY 1 IN 8 PARTICIPANTS OPT OUT OF AUTOMATIC ENROLLMENT

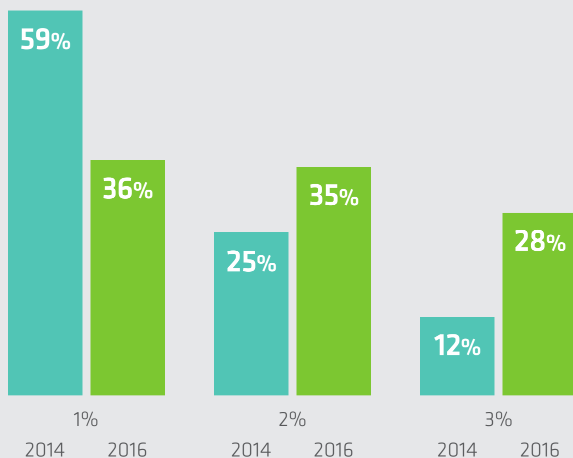
ONLY 1 IN 5 PARTICIPANTS OPT OUT OF AUTOMATIC ESCALATION

Another interesting upward trend is that more plans using auto-escalation are doing their annual increases at higher percentages. In 2014, the majority (59%) of these plans increased contribution rates by 1%. Two years later, far more plans opt for either 2% or 3% annual escalations.

This may reflect a growing understanding by some plan sponsors that the DOL has certainly given its blessing to a variety of seemingly paternalistic, automatic features in DC plans. But auto-enrollment and auto-escalation also improve plan statistics—and that may be a more notable argument for adopting them.

THOSE WHO AUTO-ESCALATE SALARY DEFERRALS BY 1%, 2%, AND 3%

% of respondents who utilize auto-escalation



Percentages will not sum to 100, as there was also an "other" category available.
Source: AB Research, 2016

PROOF-POSITIVE: AUTO FEATURES IMPROVE PLAN METRICS

Companies use a wide variety of metrics to gauge how well the DC plan is doing. These may include making participants more confident in a comfortable retirement or improving participants' knowledge of investing principles.

Those are soft numbers—it's good to see them rising, but they're difficult to accurately collect or assess. There are some hard numbers, such as employee participation in the DC plan, that tell a definitive story of improvement or decline. And the hard data says that automatic features decidedly help improve retirement readiness.

For example, most companies would like to see their DC participation rates at or above 80%. The median participation rate across all plan sizes is roughly 69%. If we break that down, we find that companies using automatic enrollment average nearly 74% in plan participation, while companies that don't use it have an average of 64%—roughly 10 percentage points lower.[8]

If we look at how many companies have achieved that sought-after 80% or higher participation rate, the numbers are, again, strikingly different. That high participation rate occurs for 37% of companies using auto-enrollment, but only for 28% of those that don't. Again, that's a gap of nearly 10 percentage points.

Auto-enrollment also paints a surprisingly different picture concerning total assets in plans. Across all plan sizes, the median for plans using auto-enrollment is over $48 million, compared to less than $9 million for those that don't.

One other interesting statistic is that 65% of sponsors using auto-enrollment say that the primary purpose of their plan is to serve as the sole retirement vehicle for most plan participants, compared to 55% of those that don't offer auto-enrollment.

8 Auto-escalation use/non-use data show similar gaps to those noted in this section.

RECALIBRATING INVESTMENT MENUS: OLD AND NEW DIRECTIONS

Some DC plans continue to tinker with the mix of their investment offerings, hoping to improve workers' retirement outcomes. But other plan sponsors want to deal directly with the limitations of participant investment knowledge by conducting reenrollments with a QDIA.

CORE INVESTMENT MENUS, MORE OR LESS

Too big? Too small? Just right? Many plan sponsors keep revising their investment menus, asking themselves what changes could generate more effective options—and outcomes—for participants. While half (52%) say their plans have the right number of investment options, another third (34%) feel the need for more. Still, 10% feel their plans have too many investment options.

The question of quantity going forward likely depends on today's tally. Nearly one-fourth of plans offer 16 or more investment options, while another 10% offer fewer than five. Most plan menus (63%) range from 5 to 15 offerings, and over two-thirds of plan sponsors say that's the right range to satisfy diversification requirements.

Nontraditional, or alternative, investments like commodities, real estate, market neutral, and long/short equities, have seen a sizable increase on plan menus, from 42% in 2014 to 66% today. Global bond offerings have remained steady, at 75%, but that may increase, now that the US Federal Reserve is raising interest rates. Global offerings, with exposure to multiple countries, provide diversification and the potential for improved returns.

BUT WHAT'S BEST FOR PARTICIPANTS?

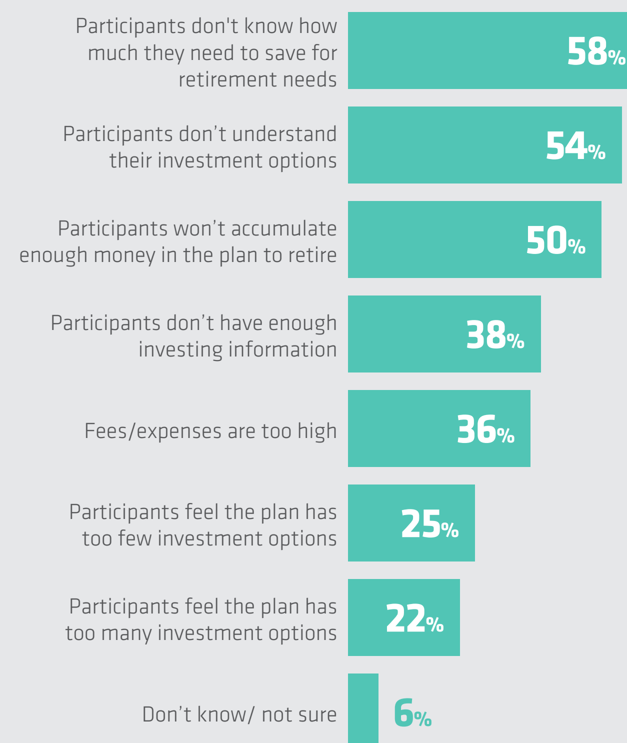
Adjusting the number and scope of the choices in a plan menu can help participants plan and save more effectively for retirement. But will that solve the chronic problems of insufficient financial literacy and low savings rates? When we asked plan sponsors what issues they were most concerned about improving, the top two answers focused on participants not knowing how much they need to save (58%) and not understanding their investment options (54%). The third-highest response was that participants won't accumulate enough money in the plan to retire (50%).

The issues of participants feeling they have too few (25%) or too many (22%) investment options pale in comparison.

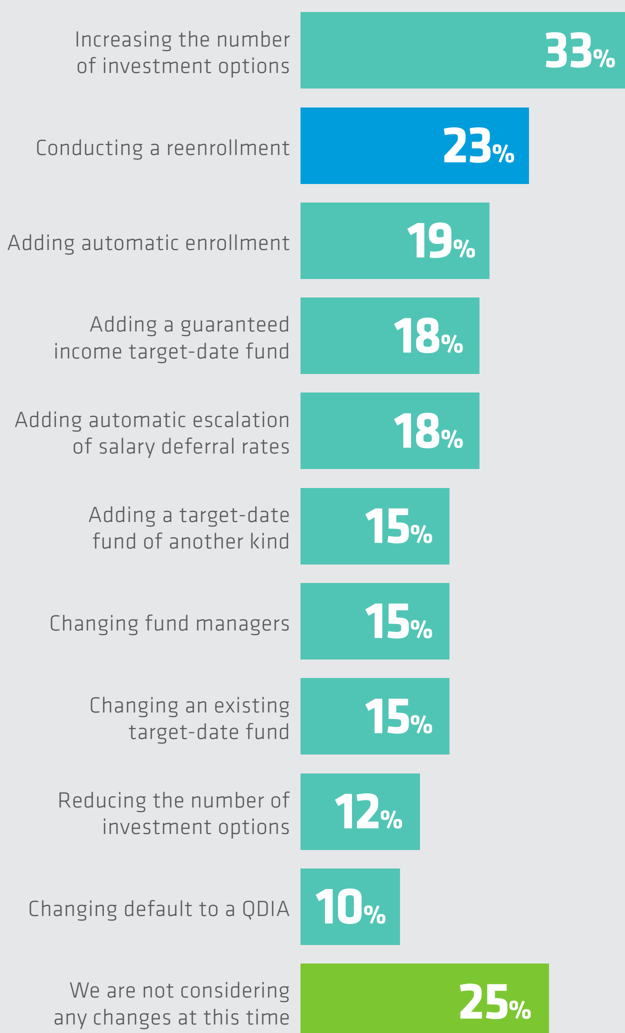
Perhaps there's a growing recognition of how hard it is to effectively educate participants about even the most basic building blocks of retirement planning and saving. That may be a major factor in how plan sponsors are approaching changes to their organization's plan design and investment options.

FROM THE CHOICES BELOW, WHAT THREE ISSUES ARE MOST CONCERNING TO YOU, AS A PLAN SPONSOR, IN TERMS OF NEEDING IMPROVEMENT?

% of respondents when asked to select the top three



Source: AB Research, 2016



While fully one-fourth of our respondents say they're not considering any changes at this time, that number is down notably since 2014.

Among the rest, who are planning to make at least one major change, the leading response is still to increase the number of investment options. That, too, is down (but just slightly) from 2014.

Interestingly, the next on the list is something new: conducting a reenrollment. That's an important plan initiative that can not only help current participants, but also effectively start nonparticipants on a practical road to retirement saving.

Other actions high on the list include adding automatic enrollment and automatic escalation. This current survey also saw an uptick in plans that are considering adding a guaranteed target-date fund. All three of these actions could greatly increase participants' retirement savings and confidence. The most effective approach for these changes? Implementing a reenrollment.

REENROLLMENTS ON THE RISE

It isn't easy to persuade plan participants to take the wheel regarding their asset-allocation decisions. While some participants actively choose investments for their account, many don't make the best choices, and some make no choices at all. That's why more plan sponsors are initiating reenrollments.

Reenrollments[9] are on the rise. In fact, 41% of our respondents say they've conducted a reenrollment during the past three years. And another 23% are considering a reenrollment in the next two years.

A reenrollment is a powerful way to steer employees into effective investment options. Typically, it's implemented with a QDIA, such as a target-date fund. Callan notes that with the large plans it surveys, 88% of reenrollments use target-date funds. At the same time, the plan can institute automatic enrollment and/or automatic escalation if it wasn't using them before. All this removes the asset-allocation guesswork and can keep participants saving—and increasing their savings rate in a gradual, reasonable way.

Reenrollments with a QDIA also provide fiduciary safe harbor that protects plan sponsors from liability against investment-related losses in participant accounts.

9 A reenrollment is defined as a process that places employees' retirement savings into a plan's QDIA on a certain date unless they make an active decision to choose another investment.

And while participants can opt out (either before or after the implementation) of the QDIA, most stay in. For example, for our respondents who conducted a reenrollment in the past three years, the median opt-out rate was only 20%. And in our experience helping clients with reenrollments, 60% to 80% of plan assets have ended up in their plan's QDIA.

ISSUES WITH CHANGE

Change is never easy, but the hardest part of a reenrollment might just be the psychological barriers. Some plan sponsors feel there's no need to do a reenrollment. That would be a reasonable response if their plans had more than 80% participation, although that's the case for less than one-third of all plans.

Another concern is negative participant reactions. But this worry may be misplaced: typically, nine out of 10 participants (90%) are happy with reenrollment, and only one in five opts out and picks his or her own investment mix. Of the participants who pick their own investments, 30% end up choosing the default investment anyway.

If the big perception hurdle is that a reenrollment is too much work or that there could be fiduciary risks, neither of those is the case. Reenrollments can be simple and inexpensive, with little effort from the participant and benefits to plan sponsors far outweighing the work in almost all cases. And if the reenrollment uses a QDIA, it's likely to improve participant outcomes without increasing fiduciary risk.

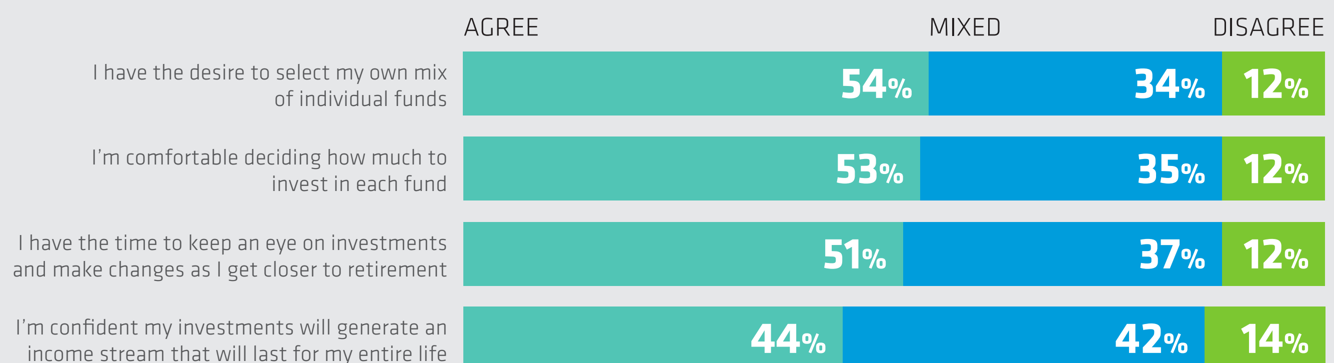
KEEPING PARTICIPANTS ON TRACK FOR HEALTHY RETIREMENT

Many participants lack the confidence to make complex investment decisions. This isn't a surprise—survey results show workers often fall short in their knowledge of investment basics.

Only about half of participants are interested in selecting their own mix of funds or are comfortable deciding how much to invest in each fund. Even fewer say they have time to track those investments and make changes as their retirement approaches.

So, it's no wonder some participants don't properly allocate their assets—especially employees who've been at a company for several years. These veterans may think their plans are in good shape because of the investment choices they made when first hired, but there's a good chance that their allocations need to be realigned.

MANY PARTICIPANTS HAVE ISSUES WITH THEIR INVESTING CAPABILITIES



Answers were on a scale of 1 to 10 with 8–10 = agree; 4–7 = mixed; 1–3 = disagree
Source: AB Research, 2017

DEFINING YOUR PLAN'S CONTRIBUTION TO RETIREMENT READINESS

The goal for DC plans and sponsors is to increase employee confidence about retiring. Today, plan sponsors have more tools to help achieve that goal.

THE LITMUS TEST FOR MEASURING SUCCESS

When we ask plan sponsors to name their top two critical measures of plan success, the top response is employees' confidence about their prospects for a comfortable retirement. The next four are mentioned substantially less often. But by and large, the top answers show that sponsors want employees to understand more and feel more prepared for living in retirement.

We've noted several ways that plans can augment and improve retirement saving (and confidence):

+ offering financial wellness programs
+ adopting a QDIA, such as a target-date fund, and implementing a company-wide reenrollment
+ diversifying core-menu bond options with global bonds
+ incorporating some alternatives—possibly through a more sophisticated target-date fund glide path
+ adopting automatic enrollment and automatic escalation.

As might be expected, plans that already use automatic enrollment have typically seen greater increases in plan participation than those without auto-enrollment. And decreases in plan participation are slightly higher for those without auto-enrollment. But what's interesting is that when plan participation decreases, sponsors are even more keen on "having employees feel confident about their prospects for a comfortable retirement" as a top measure of the plan's success. Auto-enrollment can move that off the wish list and onto the chart of accomplishments.

WHICH OF THE FOLLOWING DO YOU FEEL ARE THE TWO MOST CRITICAL MEASURES OF SUCCESS FOR YOUR ORGANIZATION'S PLAN?

% of respondents

Measure	%
Having employees feel confident about their retirement prospects	46%
Improving employee understanding of investment options	33%
Improving employee understanding of how account balance may translate into annual income stream	33%
Offering investments that consistently outperform their benchmarks	32%
Improving participation	31%
Reducing plan fees	25%

Source: AB Research, 2016

FINANCIAL ADVISORS/CONSULTANTS

But to act confidently on adding these confidence-building tools, companies may need to improve their fiduciary training for plan sponsors.

One factor that can help is to enlist the assistance of a financial advisor or consultant (we'll refer to them collectively as financial advisors). Many larger plans have access to in-house teams as well as additional outside resources. Smaller plans don't, so the help of a financial advisor can have significant benefits—for plan sponsors as well as participants.

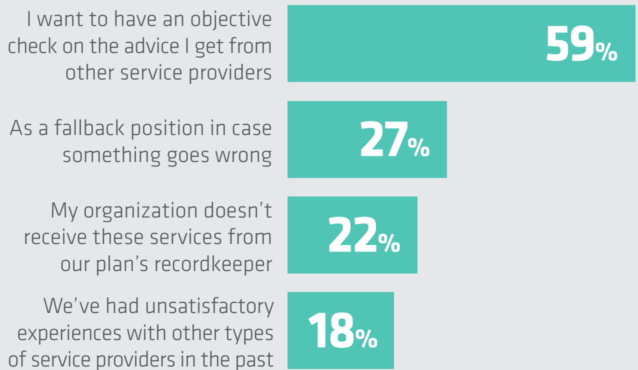
Of respondents whose plans have less than $50 million in assets, over 80% say they use a financial advisor. Nearly as many (73%) say it is important or very important to them to have a financial advisor act as a fiduciary.

When we ask respondents why, the most frequently cited reason (59%) is to have an objective check on the advice they get from their plans' other service providers. What plan sponsors most value about using a financial advisor is that they provide quality investment advice and guidance (57%). Just over half of sponsors who use financial advisors feel another valuable aspect is that the fees are reasonable for the services received.

On many metrics for plan success, those micro to midsize plans that use financial advisors fare much better than plans that don't use advisors. More plans using advisors show healthy participation rates, increased participation in the last three years, higher average savings among participants and more participants improving their retirement readiness.

KEY REASONS FOR USING A FINANCIAL ADVISOR/CONSULTANT

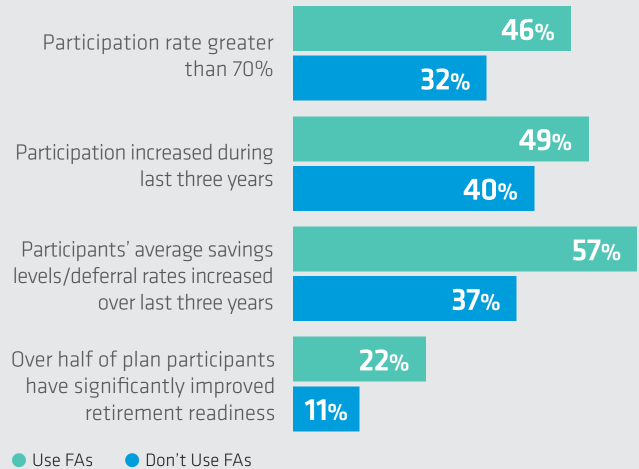
Why do you currently use a financial advisor/consultant for investment or fiduciary services? (% of plans with less than $50 million in assets)



Source: AB Research, 2016

METRICS ON PLAN SUCCESS

Comparison of results for plans using financial advisors/consultants (FAs) vs. plans not using them (among DC plans with less than $50 million in assets)



Source: AB Research, 2016

APPENDIX

A. WHY YOUR DEFAULT INVESTMENT MATTERS

Qualified default investment alternatives (QDIAs) are capturing most of the assets of younger savers today. And many in the industry expect that within 10 years, QDIAs will likely account for the vast majority of DC plan assets.

DEFAULT NECESSITIES AND REPERCUSSIONS

When participants don't choose an investment option for their plan assets, most DC plans automatically invest those assets in a default investment option. Before the Pension Protection Act of 2006 (PPA) and subsequent regulations in 2007, plan sponsors didn't have safe harbor protection from fiduciary liability for any default investment option. So they typically employed extreme caution and used low-risk/low-return options that were unlikely to lose money.

The PPA has changed that by extending fiduciary safe harbor protection to QDIAs that "include a mix of asset classes consistent with capital preservation or long-term capital appreciation or a blend of both." The Department of Labor (DOL) clarified this in 2007, giving the safe harbor nod to three types of diversified options: a target-date retirement fund product or model portfolio; a target-risk fund or model portfolio (such as a balanced fund); or an investment-management service that allocates a participant's assets among the plan's alternatives based on the participant's age, target retirement date or life expectancy. The DOL also lets plans use stable-value or money-market funds as a temporary QDIA, but only for the first 120 days after an employee begins contributing.

Default safe harbor protection applies to many situations when a participant doesn't provide investment direction, including automatic enrollment; when plans eliminate an investment option or there's a change in service provider; or when a participant rolls over assets from another plan without indicating an investment choice for those assets. The QDIA safe harbor and other government-sanctioned encouragements can help only if plan sponsors are aware of them.

THE BENEFITS OF QDIAS

Not only do QDIAs provide safe harbor protection for plan sponsors, but these investment vehicles also often provide better asset allocation for participants than they might construct on their own. As more plans continue to adopt automatic enrollment, the selection of a default option will increase in importance.

B. HOW WE DEFINE A GUARANTEED STREAM OF INCOME

A guaranteed stream of income, as we define it in our survey, would be based on a percentage of a participant's higher account balance in the years leading up to retirement. It would give participants

+ an income stream that will last as long as they live
+ the potential to increase the size of their income stream with gains in investments
+ income protection in down markets because the size of the secure, guaranteed payments will never decrease
+ the flexibility to take all or part of their money out of their account at any time without incurring withdrawal fees

C. HOW WE DEFINE TARGET DATE

"Target date" in a fund's name refers to the approximate year when a plan participant expects to retire and begin withdrawing from his or her account. Target-date funds gradually adjust their asset allocation, lowering risk as a participant nears retirement. Investments in target-date funds are not guaranteed against loss of principal at any time, and account values can be more or less than the original amount invested—including at the time of the fund's target date. Also, investing in target-date funds does not guarantee sufficient income in retirement.

HOW WE DEFINE "CORE STANDARDS OF CONDUCT" FOR FIDUCIARIES

+ To act solely in the interest of plan participants and beneficiaries, with the single purpose of providing benefits to them
+ To pay only necessary and reasonable expenses for administering the plan
+ To perform duties with the care, skill, prudence and diligence of a person knowledgeable in the field
+ To minimize the risk of large investment losses by offering a diversified menu of investment options
+ To adhere to the terms of the documents governing the plan and ensure that these documents comply with ERISA
+ To not engage in self-dealing and to avoid conflicts of interest

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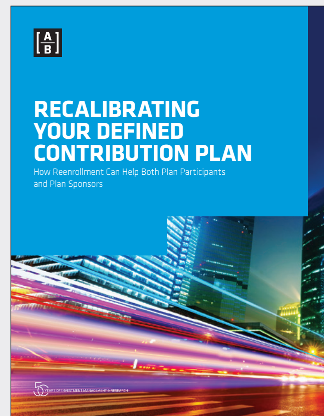
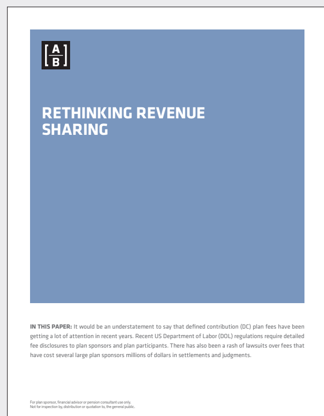
What's Old Is New Again—Collective Investment Trusts Reduce DC Plan Costs

Inside the Minds of Plan Participants

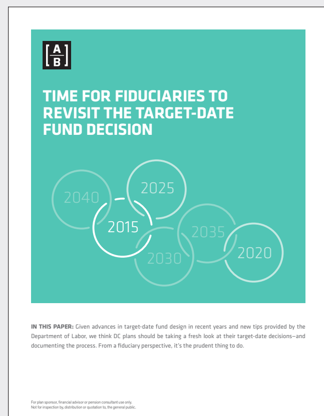


Recalibrating Your Defined Contribution Plan—How Reenrollment Can Help Both Plan Participants and Sponsors

Across the Universe—How Global Bonds Meet the DC Core Objective



Rethinking Revenue Sharing



Time for Fiduciaries to Revisit the Target-Date Fund Decision

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17-0605093312
DCI–6150–1117
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