



Investment Platform Options that Can Lead to Better Retirement Outcomes

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As plan sponsors become more attuned to the importance of retirement readiness, there is an increasing focus on finding ways to leverage plan design to help participants get the best possible retirement outcomes. The focus on measuring “outcomes” – enabling participants to retire with adequate savings – has steered the retirement industry toward developing plan design solutions as the answer to common retirement challenges.

If retirement readiness is considered a sound measure of retirement plan success, plans built with the intent to better prepare current and future generations of employees for more successful outcomes may be the answer. It is through a combination of actions that participants can better their chances of getting retirement ready: saving over the long-term, deferring at a rate that will meet savings goals, and using a diversified investment strategy to manage risk. With an optimized plan and investment menu design, participants may be able to overcome many retirement planning challenges.

In this paper, we will explore how better plan design, and specifically, how making appropriate and the best possible investment solutions available to participants, can drive retirement readiness and plan success.



A Changing Plan Environment

A Shift from Retirement Asset Accumulation to Distribution

Since 2011 when the first of the Baby Boomer generation turned age 65, retirement plan contributions have begun to trend lower and benefit payments have trended higher, according to an analysis of US Census data. Although retirement plan contributions for the Baby Boomer generation are still largely in the accumulation stage, data from Retirement Research, Inc. finds a shift to net distribution has begun. In Figure 1, as the population ages, those ages 45 through 64 in the prime accumulation stage will gradually begin to decrease from a high of 25.1 percent in 2020 to 24 percent in 2060. In contrast, the population drawing retirement assets starting at age 65 will increase – from 16.9 percent in 2020 to nearly meet the declining population in the accumulation stage in 2060 at 23.6 percent.

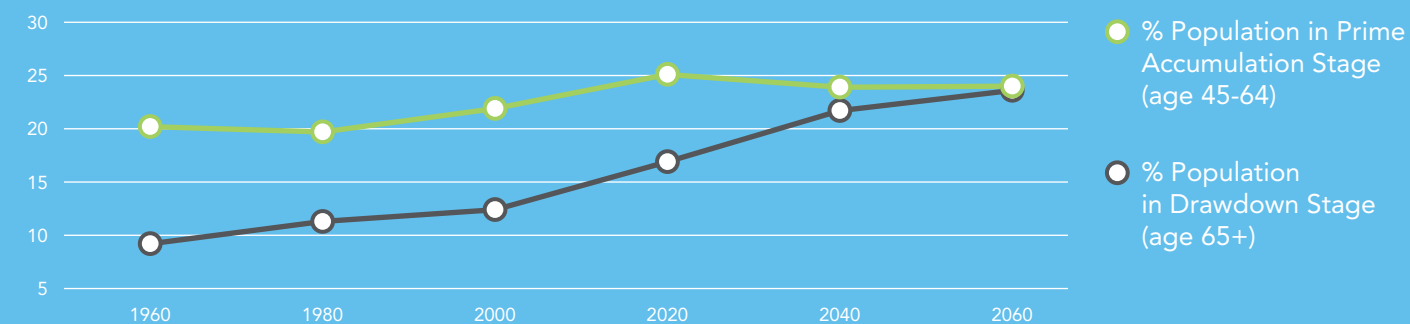
Although approximately 40 percent of employee account balances normally remain in plans when participants retire, more than half of these assets typically leave the plan within five years.¹ In addition, those nearing retirement generally have larger balances than younger workers who are earlier in the retirement accumulation stage. Therefore, it is expected that future contributions will continue to decline, and benefit payments will rise with the aging of the population.

While the Baby Boomer generation may not have had access to a 401(k) plan throughout their career, younger generations can benefit from the savings opportunity these plans offer. 401(k) plan design has evolved to make a number of services and features available to plan sponsors that can improve employees' retirement preparedness.

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Figure 1 - The Effects of an Aging Population



Source: Analysis of U.S. Census Bureau actual and projected population statistics, 2014.

¹ Brightwork Partners, Survey of Recently Retired Defined Contribution Participants. December 2013.

Measuring Beyond Plan Participation

Building Better Outcomes through Better Plan Design

Participants need guidance to make better retirement planning choices. And building better retirement outcomes through better plan design – such as with automatic plan features that nudge participants toward better planning decisions – have become vital to better preparing Americans for retirement. It is a combination of many factors, as illustrated in Figure 2, that contribute to a participant's retirement readiness, including contribution rate, age appropriate asset allocation, and loan or withdrawal usage. As Figure 2 also illustrates, plan features and tools have been developed to target and improve results specific to these factors.

Figure 2 - Features Driving Retirement Readiness

Goal	Tools
Increasing participation	▶ Automatic enrollment ▶ Targeted communications ▶ Onsite mobile applications (iPads)
Increasing contributions	▶ Automatic deferral escalations ▶ Targeted communications ▶ Mobile applications ▶ Stretching the match
Improving age appropriate asset allocation	▶ Target date funds ▶ Advisor designed model portfolios ▶ Managed accounts ▶ Greater access to investment advice
Focusing on retirement income	▶ Income gap reporting ▶ Retirement income planning tools ▶ In-plan retirement income products ▶ More options at distribution ▶ Providing retirement planning to pre-retirees
Preserving assets for retirement – reducing leakage	▶ Targeted communications to discourage cash outs ▶ Tightening in-service withdrawal provisions ▶ Eliminating loans or reducing the number of loans available
Increasing the % of participants on track to achieve an acceptable income replacement ratio	▶ Income replacement education and modelling tools ▶ Gathering information about the totality of household's sources of retirement income, not just participant balances and age

Source: RRI Vendor Profiles January 2015.

Since the Pension Protection Act of 2006, automatic enrollment has been more widely adopted, and according to plan sponsor surveys conducted by the Plan Sponsor Council of American (PSCA), the percentage of plans using automatic enrollment has grown from 36 percent in 2007 to 50 percent in 2013, with the greatest usage among plans with more than 1,000 participants (over 60%).² The use of automatic plan design solutions like automatic enrollment can get employees saving that otherwise may not do so until a later date. Automatic contribution increases can bump savings levels up to build account value.

² PSCA 57th Annual Survey of Profit Sharing and 401(k) Plans, Plan Sponsor Council of America. October 2014.

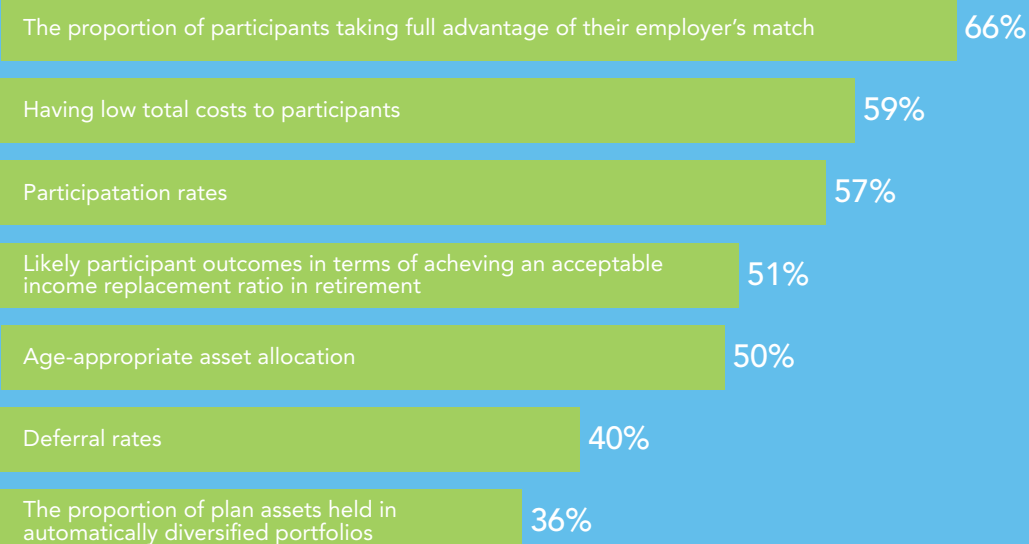
And diversified, age targeted investment options like target retirement date funds provide a simple solution for what is often considered the most difficult part of retirement planning: choosing investments.

However, whether a plan uses an automatic savings design structure or not, fiduciary decisions such as investment menu choice and monitoring, plan Qualified Default Investment Alternative (QDIA), and fund fees are important to retirement outcomes. Plan investments should seek to maximize growth, manage risk, and charge reasonable fees. And, generally, it can be expected that participants with access to a low cost investment menu that meets their needs and realizes plan performance requirements will have better investment outcomes than those that do not.

When evaluating retirement plan effectiveness, financial professionals agree that it is critical to measure beyond plan participation rates. Participant outcomes, costs, and an investment menu that allows appropriate diversification also matter. As noted in the Brightwork Partners, LLC study referenced in Figure 3, in addition to participation and deferral rates, financial advisors view low costs, participant outcomes, and appropriate diversification as components that matter “a great deal” to retirement plan success. Plan-level reporting that measures and benchmarks plan effectiveness has become a major feature offered by many providers. Data like the number of participant investment holdings, target date fund utilization, and assets by investment provide insight into whether participants are investing to meet goals and manage risk.

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Figure 3 - Evaluating Plan Effectiveness



Source: Brightwork Partners, LLC January 2015.

Open Fund Architecture Platforms

Driving Better Investment Outcomes

Plans looking to create better investment outcomes may want to consider retirement plan investment solutions like open fund architecture platforms, target retirement date funds, pre-selected portfolio platforms, 3(21) and 3(38) fiduciary services, and zero revenue sharing funds. These solutions support better investment outcomes with a plan investment menu that is built for the following objectives:

- ▶ Selected to meet the needs of all participants
- ▶ Helps participants manage risk and maximize growth
- ▶ Realizes plan performance requirements
- ▶ Charges low fees
- ▶ Is diligently screened and closely monitored



Open Fund Architecture Offers a Flexible Foundation for Building an Investment Menu

In recent years, many retirement plan providers have moved from set investment line-up approaches to a less structured open fund architecture style. In the past, this unstructured approach has afforded plan sponsors the freedom to select investment funds from across asset managers. However, with recent fee and fiduciary focus, this platform has become even more attractive for the flexibility it offers. An open solution can be the cornerstone from which plan sponsors fulfill their fiduciary responsibilities – through access to a broad universe of investment choices from which they can build a diverse investment line up of funds that meet the needs of all plan participants, fulfill performance criteria, and charge reasonable expenses.

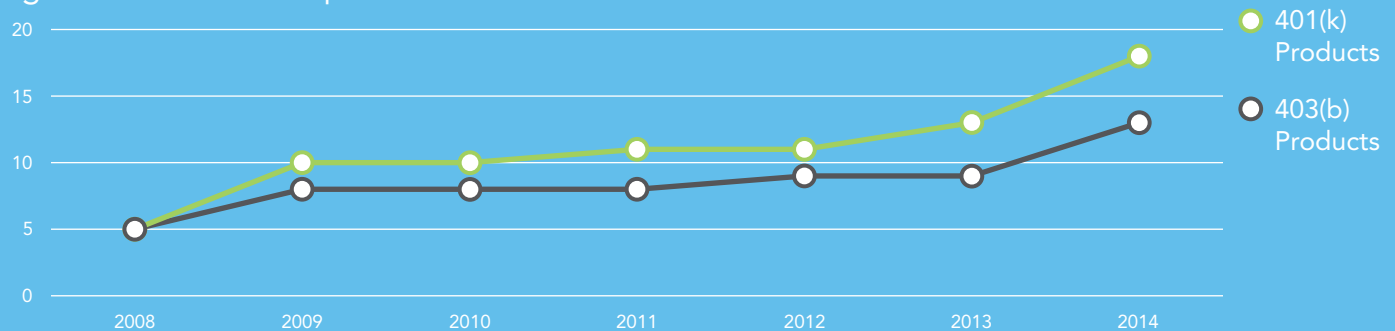
RRI data finds that an open platform:

- ▶ Can be modified to fit multiple service tiers by offering a range of service models and flexible advisor compensation to meet plan needs.
- ▶ Allows multiple investment platforms, such as R2 through R6 investment share classes that charge low to no investment fees, within a single product each with a single share class equivalent line-up of proprietary funds and non-proprietary funds.
- ▶ Can include true institutional funds, collective investment trusts (CITs) and exchange-traded funds (ETFs).
- ▶ Registered Investment Advisors (RIAs) often select no load and zero revenue sharing funds for use in defined contribution plans

Since 2008, there has been a growth trend of open fund architecture products in the 401(k) market – the number of platforms tracked by RRI has more than tripled to 42 percent of all products. These platforms are also becoming increasingly available in the under \$5 million market, slowly displacing tight due diligence platforms and group annuity products with more limited selection according to RRI data.

Plans that start with an open fund architecture as their investment foundation have the freedom to build an investment lineup from an extensive number of investment options. However, plan sponsors who are not well versed in selecting and monitoring investments may want to also consider other solutions, such as due diligence investment platforms and fiduciary services.

Figure 4 - Growth of Open Fund Architecture Platforms



Source: RRI Vendor Profiles January 2015.

Due Diligence Investment Platforms

Due Diligence Investment Platforms Include Screening and Monitoring Services

Due diligence investment platforms can be a simple, effective solution to building the plan portfolio. These platforms offer a menu of pre-screened investment portfolios built to address specific participant and plan cost requirements. They have typically undergone a defined due diligence process and are regularly monitored through standardized reporting available through the provider. Due diligence investment platforms can aid investment outcomes because they offer: sufficient fund choice, a defined due diligence process, reasonable costs, and less work and risk for the plan sponsor.

Target Retirement Date Funds are an Automatic Investment Solution that Manages Risk

Wider use of auto features is largely responsible for the increased utilization of target retirement date and asset allocation funds. Target date funds have become the dominant Qualified Default Investment Alternative (QDIA) for auto enrollment plans, with usage rising from 57% in 2009 to 72% in 2013 for all such plans according to RRI data. The growth of target date fund assets reached \$750 billion in 2014 as noted in Figure 5, a large increase from the \$200 billion shown in these funds in 2008. This growth is likely to continue as more plans adopt auto features and plans expand them to include an automatic contribution step-up component.

Whether a plan uses an automatic plan design or not, target retirement date funds provide a solution to what many consider the most difficult retirement planning decision participants face – choosing investments. These funds provide a simple, risk appropriate solution based on a participant's age and adjusts or rebalances over time in accordance with the fund strategy. When used appropriately, they potentially offer participants a better investment outcome by managing risk through a diversified age-based allocation that automatically adjusts over time.

Across all 401(k) plans, participant asset allocation balances in target date funds have steadily increased from 6.6% in 2008 to 15.3% in 2013, according to research by the Employee Benefit Research Institute (EBRI).³ These allocations vary widely by age with younger participants leading in target date fund utilization: participants in their 20's allocated 35 percent of their balances to target date funds, participants in their 30's allocated 23 percent, and participants in their 60's allocated just 13 percent of their balances to target date funds.⁴

Figure 5 - Target Date Fund Asset Growth

Year	Assets (billions)			As a % of All DC Plan Assets*
	Risk-Based Asset Allocation Funds	Target Date Funds	Total	
2008	\$115	\$200	\$315	9.3%
2010	\$145	\$390	\$535	11.7%
2012	\$145	\$510	\$655	12.7%
2014	\$165	\$750	\$915	13.9%

* Risk-based asset allocation funds and age-based target maturity date funds held in Corporate DC, 403(b) and 457 plans.

Source: RRI Vendor Profiles January 2015.

³ EBRI, Issue Number 408. December 2014.

⁴ Kevin McGuinness, "401(k) Participants Choose TDFs," Plan Sponsor Magazine, February 2014: Page 16.

Investment Fiduciary Support

Fiduciary Services Can Improve Investment Selection and Monitoring and Lower Fees

Given ERISA’s “prudent expert” requirement, plan sponsors may consider hiring a professional with the knowledge to carry out fiduciary functions they may lack the expertise to perform themselves, like choosing and monitoring investments. A qualified, outsourced expert who is responsible for providing assistance or overseeing the development of the plan’s Investment Policy Statement (IPS) and ensuring its provisions are followed, benefits both the plan fiduciary and plan participants by managing liability while improving plan effectiveness. Outsourcing specific areas of fiduciary responsibility through 3(21) and/or 3(38) fiduciary support services offer benefits to participants such as better investment offerings and monitoring of investment performance, more rapid investment changes, and lower investment management fees. It can also provide plan sponsors with some protection, increased objectivity and fewer conflicts of interest.

Open fund architecture platform plans may find fiduciary support vitally important to creating and maintaining the plan’s investment menu. Plan sponsors can choose a limited support solution like a 3(21) fiduciary who can offer investment guidance, or appoint a 3(38) investment manager to control the selection and monitoring of the plan investments. Figure 6 compares ERISA 3(21) support to the scope of the 3(38) fiduciary. Optional third party 3(21) and 3(38) services are now available on most retirement plan platforms, to address the needs of sponsors and advisors who may want to outsource such services. Our research finds this approach is gradually replacing the traditional provider’s due diligence platform. While these services can provide some fiduciary protection, plan sponsors are always ultimately responsible for the prudent selection and monitoring of the selected fiduciary.

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Figure 6 - Fiduciary Services

3(21) Fiduciary Service Features	3(38) Fiduciary Service Features
▶ States in writing co-fiduciary status ▶ Assists in drafting IPS ▶ Helps design initial fund menu ▶ Provides monitoring data ▶ Recommends changes ▶ Recommends mapping strategies ▶ Provides documentation	▶ States in writing co-fiduciary status ▶ Drafts IPS ▶ Builds initial fund menu ▶ Monitors fund menu ▶ Makes changes to fund menu ▶ Determines mapping strategies ▶ Provides documentation

Zero Fee Investment Platforms

Zero Revenue Sharing Fund Platforms Provide Choice with a Best-Possible Fee Arrangement

Helping participants pay reasonable plan expenses can potentially save them thousands of dollars at retirement. Zero fee investment platforms support the plan fiduciary's obligation to act in the best interest of participants and offer a prudent investment lineup. The model has the advantages of a variety of choice with a best possible fee arrangement for the participant. Investments on this type of platform typically pay no 12b-1, sub TA or shareholder servicing fees or compensation in general. A zero fee structure can also offer: the flexibility of customization of the investment lineup, no-fee investments, and pre-screening and monitoring services.

Conclusion

As fiduciaries, plan sponsors want to ensure they are helping participants succeed at becoming retirement ready. Many are increasingly turning to automatic plan design features as the solution to better retirement outcomes for employees. A plan that meets the needs of participants and addresses common obstacles to saving can better position participants for future financial security.

Retirement outcomes are increasingly becoming the measure of plan success – and a plan investment menu that is designed to maximize growth and manage risk, at a reasonable cost – can improve the likelihood that participants will achieve an acceptable level of income replacement in retirement. Plan sponsors seeking better retirement outcomes for their participants may want to consider investment solutions like open fund architecture platforms, target retirement date funds, pre-selected portfolio platforms, 3(21) and 3(38) fiduciary services, and zero revenue sharing funds.



Investment Platform Options that Can Lead to Better Retirement Outcomes

An open, flexible investment platform supports better retirement outcomes in three ways:

1. It provides the opportunity for plan sponsors to build an investment lineup that meets the needs of all plan participants from a large universe of fund options,
 2. It offers a wide variety of choice in low cost investment options, and
 3. It allows plan sponsors to maintain investment performance standards by enabling underperforming investment options to be quickly and easily replaced with better performing investments.
- ▶ Other plan customizations can be built upon the foundation of an open platform, including automatic investment solutions like target retirement date funds, and better fee arrangements through zero revenue sharing funds, multiple share classes, CITs, and ETFs.
 - ▶ Plans with a straight open fund architecture solution may also want to consider outsourcing areas of fiduciary responsibility through 3(21) and/or 3(38) fiduciary support services or using a due diligence platform to manage and oversee functions.
 - ▶ Generally, it can be expected that participants with access to a low cost investment menu that meets their needs, is monitored closely, and realizes plan performance requirements will have better investment outcomes than those that do not.

Making Retirement Work Better

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