The Target-Date Connection

Finding the Right Fit for Your Plan

- What's the best way to connect your plan participants with the advantages of target-date funds?
- You need an effective implementation strategy that can overcome participants' uncertainty and inertia.
- Inside: explore three implementation strategies and see which one best fits your plan—and your participants.

AllianceBernstein
Defined Contribution Investments

Target-Date Implementation: The Fiduciary Aspect

The standards continue to evolve for how defined contribution plan fiduciaries are measured. When including target-date funds in your plan, you'll be making two key fiduciary decisions: which funds to offer and the implementation strategy used to introduce them into the plan. And even though the Department of Labor has included target-date funds as a qualified default investment alternative (QDIA), there are still gray areas concerning some safe harbor limitations—no matter which implementation strategy you choose. Sponsors should make a prudent decision by evaluating their overall workforce and the current asset allocation of participants. Talk with your legal counsel before making your decision.

Connecting Participants with the Benefits of Target-Date Funds

Most participants need—and want—help with retirement investing. Target-date funds have benefits that can help, but *how* do you connect them with your participants? Choose an implementation strategy that fits your plan…and your participants.

New Horizons for Your Plan

You're considering offering target-date funds in your plan. But what's the best way to introduce them? The implementation strategy you choose can make a big difference in getting employees into target-date funds—especially the many participants who aren't comfortable with investing.

You might think that participants would jump at the chance to invest in target-date funds, with their professional asset management, all-in-one diversification, and gradual adjustment to a more conservative asset mix as participants move toward—and through—retirement.

But our research shows that less than one-third of plan participants choose target-date funds when they're available. When they do, they often put less than 40% of their assets into them—creating overlap with their other plan investments.* This can work against target-date funds' carefully designed asset mix.

Overcoming Participants' Inertia

Some plan sponsors believe they can rely on employee communications to help improve retirement savings outcomes. While that's important for new employees, existing participants have a different problem—inertia. The "I'll get to it tomorrow" attitude holds them back.

It's your implementation strategy that can have the most impact on connecting existing participants with the benefits of target-date funds. We'll explore three different approaches and give you a case study for each—real companies that we've worked with. They'll help you evaluate which strategy might work best for your plan.

The more you help your participants, the better their chances of reaching the retirement savings outcomes they want. Talk to your legal counsel as you evaluate which target-date implementation strategy is right for your plan.

*Source: AllianceBernstein research, 2008

Add-to-Menu Strategy

You can simply add target-date funds as an investment option in your plan. You may even "map" investments into them when you eliminate other investment options. But will this do enough to combat inertia?

Target-Date as Another Investment Option

It's hard for any new investment options to gain traction with participants, even target-date funds. That's because of uncertainty and inertia—participants either don't know what to do or don't want to think about it. If existing participants have to choose to invest in target-date funds, the adoption rate will typically be low. And even if target-date funds are the default option for new participants, this may not help existing participants.

A Case in Point: Regional Healthcare Institution

$150 million DC plan with 3,500 participants

The company wanted to place greater emphasis on its defined contribution plan and close its pension plan to new employees. At the same time, the company was embarking on extensive changes to its DC plan—switching recordkeepers and replacing most of the existing funds with similar ones and eliminating others.

The company decided to include target-date funds as the plan's new default option—replacing the existing default option, a stable value account, and giving the plan sponsor a "safe harbor" QDIA. But with so much happening at once, the company decided to map current assets to similar investments. Although target-date funds were added to the plan's new investment menu, no existing assets were mapped into them.

The company thoroughly communicated all the changes with brochures, postcards, e-mails and employee meetings. Although introducing the target-date funds was just one aspect, employees received extensive information about how they work and their benefits. But if employees wanted to invest in target-date funds, they had to actively choose them.

The expected result for the Add-to-Menu strategy is typically less than 2% of plan assets invested in target-date funds.

Limited Adoption of Target-Date Funds

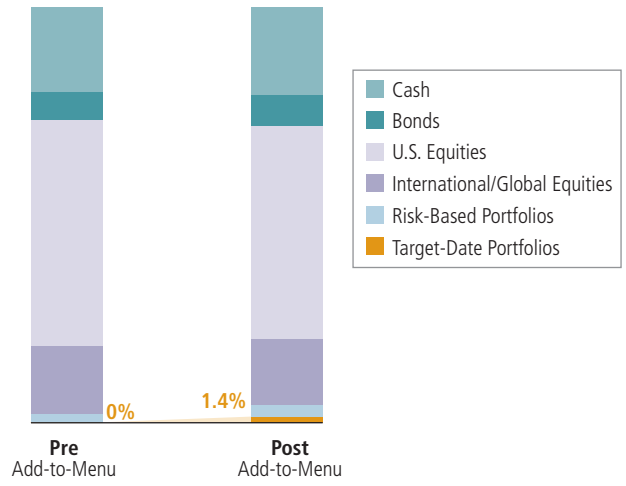
One year after the plan conversion to the new recordkeeper, target-date funds held less than 2% of the total plan assets. Our experience tells us that 2% or less is a typical result for the Add-to-Menu strategy. That's because participant inertia usually keeps investors from actively choosing any new fund—even target-date funds.

The company replaced most of its existing funds with reasonably similar ones. Since the company simply added target-date funds to the lineup of investment options, participants had to proactively elect them. So in this case study, the plan's asset allocation barely changed—and cash still played a prominent role.

Generally, the Add-to-Menu strategy falls short of getting participants invested in the target-date funds. It also won't help much with improving participant-level asset allocation.

The Add-to-Menu strategy doesn't help overcome inertia.

Add-to-Menu Strategy Percent of Plan Assets



Source: AllianceBernstein

Timing and Other Points to Consider*

The Add-to-Menu strategy typically takes between 45 and 90 days to implement, but you should allow more time to notify participants if you're changing your investment menu. Make sure you notify your recordkeeper of your desired "live" date in advance.

Once the funds are available, you should consider sending additional announcements to eligible employees—describing how target-date funds work, their benefits and how employees can take action. Also consider conducting employee meetings after the funds go live—building on the meetings' enthusiasm and momentum during a time when participants can act immediately.

* Timing varies by implementation strategy for each plan and recordkeeper—you'll need to take various factors into consideration. It's important to discuss implementation timing and capabilities with your recordkeeper to set proper expectations.

Investment Re-election Strategy

Another approach is to turn the investment-election process on its head: require participants to re-evaluate their current investment elections and take action to keep them. If they don't take action, place their assets in the appropriate target-date fund.

Re-election: Accommodating All Participants

Our research shows there are two basic types of participants. The majority are Accidental investors who lack investing confidence and worry about retirement planning. Others are Active investors who feel confident and enjoy investing. Plan sponsors often look for a target-date implementation strategy that will accommodate both types of participants.

The Investment Re-election strategy respects the independence of Active investors while also providing a "helping hand" to Accidental investors.

A Case in Point: Large Financial Services Firm

$700 million DC plan with 5,000 participants

The company was making several plan enhancements and used the conversion process as a catalyst to ensure better asset allocation for participants.

The plan sponsor knew that the company had many participants who were unsure and lacked confidence in investing, but the company also had confident, involved investors as well. The sponsor didn't want to mishandle either group.

So the company chose to use the Investment Re-election strategy as part of a plan conversion. This approach required all participants to make new investment elections—for existing balances and future contributions. If participants didn't choose within a specified period of time, the strategy placed their assets into the appropriate target-date fund.

The plan conversion included a full suite of communications—newsletters sent to employees' homes, a series of e-mails (and reminders), education meetings, and an easy-to-use online investment selection process. And throughout the process, the communications made a strong case that target-date investing was a better path for participants who didn't have the time, desire or confidence to make their own investment mix.

The expected result for the Investment Re-election strategy is typically 50% to 80% of plan assets invested in target-date funds.

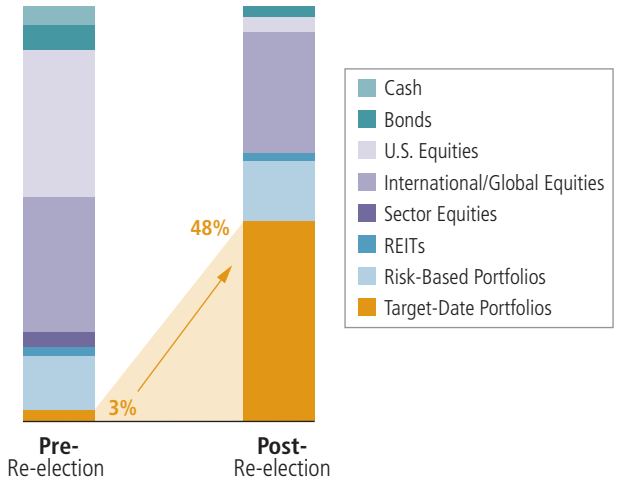
Satisfying Results for Both Investor Groups

Before the company underwent the plan conversion with the Investment Re-election strategy, target-date funds accounted for only 3% of its total plan assets. Afterward, target-date funds jumped to almost 50% of plan assets. Our experience tells us that between 50% and 80% is a typical result for the Investment Re-election strategy. The company also received positive informal feedback from its employees. In fact, many of its Active investors appreciated the effectiveness of the target-date option and became target-date converts.

The Investment Re-election strategy boosts the use of target-date funds by participants—whether they avoid decisions due to uncertainty, reluctance or inertia. It reverses the election process and turns obstacles into advantages. It also helps improve participant-level asset allocation, providing more thoughtful and age-appropriate diversification than most Accidental investors typically construct on their own.

The Investment Re-election strategy helps overcome inertia—even for employees in investment companies.

Investment Re-election Strategy Percent of Plan Assets



Source: AllianceBernstein

Timing and Other Points to Consider*

The Investment Re-election strategy typically takes between 120 and 180 days to implement. Eligible employees need to make investment elections by a specified date, so your communications materials must be prepared and distributed prior to the beginning of the investment "re-election window." You should also consider when you'll hold education meetings—whether it's before or during the re-election period.

Make sure you give participants enough notice about the changes and when they'll occur. You'll need to notify participants before the re-election window and again at least 30 days before assets are moved. Also, make sure your recordkeeper can support the defaulting, or "negative" election process, during your re-election window.

The Department of Labor has indicated that when plans use the Investment Re-election strategy, plan fiduciaries may be protected from fiduciary liability under a "safe harbor" in the final default investment regulations if the participant notice and other requirements of the regulations are properly followed. Be sure to consult your legal counsel who can guide you through the regulations and the steps you'll need to take.

* Timing varies by implementation strategy for each plan and recordkeeper—you'll need to take various factors into consideration. It's important to discuss implementation timing and capabilities with your recordkeeper to set proper expectations.

Investment Reset Strategy

At some companies, plan participants need as much retirement investing help as they can get. When that's the case, the Investment Reset strategy moves all assets into target-date funds first, and only afterward lets participants actively choose other options.

A Fresh Start in Target-Date Funds

The Investment Reset strategy is the boldest approach to implementing target-date funds. First, communicate the upcoming changes to participants. Then, move all participant assets into target-date funds based on their age. After, allow participants to move their assets out of target-date funds and into other investment options. Even with the option to move out of target-date funds, most participants—including many actively involved ones—stay.

The Investment Reset strategy results in a greater percent of plan assets in target-date funds than other strategies—whether it's because of inertia or participants realizing the benefits of target-date funds. This fresh-start approach uses Accidental investors' inertia to their own advantage, but it still allows participants to choose other options after the transition date.

A Case in Point: Specialty Food Distributor

$96 million DC plan with over 1,000 participants

The company was preparing to switch its DC plan recordkeeper. But the plan sponsor also needed to solve several key problems—especially the fact that participants were allocating their assets poorly. With the vast majority of employees being Accidental investors, more than half of the plan's total assets were concentrated in large-cap growth stocks and cash.

The company wanted to do the right thing for as many employees as possible, so it decided to thoroughly revamp its plan. The company switched recordkeepers, instituted automatic enrollment, changed the fund lineup and added target-date funds as the default investment option.

Employees received a full array of communications: all plan assets were moving into target-date funds and participants could choose other investment options after the plan conversion. Education meetings provided more information about target-date funds, the benefits of diversification, enrollment procedure details and how to change investment direction after the plan conversion.

The expected result for the Investment Reset strategy is typically 80% to 95% of plan assets invested in target-date funds.

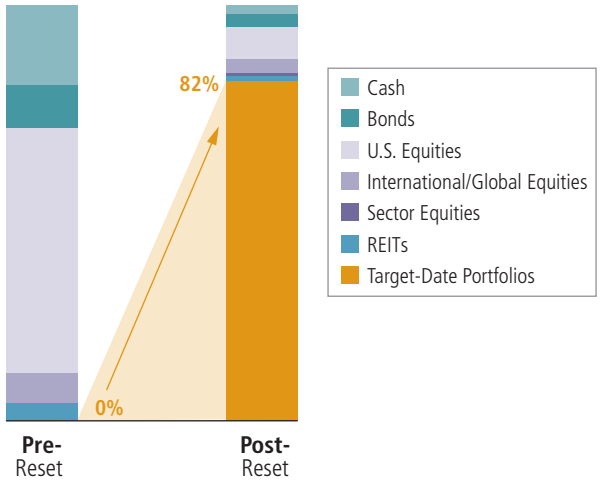
Reset Result: The Vast Majority Stick with Target-Date Funds

One year after the conversion, over 80% of the plan's assets remained in target-date funds. Our experience tells us that between 80% and 95% is a typical result for the Investment Reset strategy. That's because this strategy uses inertia to participants' greatest advantage.

The company's decision to implement target-date funds with the Investment Reset strategy gave many employees a more reasonable, age-appropriate asset allocation. Now, rather than starting on an investing path of confusion, uncertainty and inertia, many participants were given a better chance for better outcomes.

The Investment Reset strategy uses inertia to your participants' greatest advantage.

Investment Reset Strategy Percent of Plan Assets



Source: AllianceBernstein

Timing and Other Points to Consider*

The Investment Reset strategy typically takes between 60 and 90 days to implement, but you'll need more time if your plan's going through a recordkeeping conversion.

You should verify that your recordkeeper can process the transition during your proposed timeframe. Consider conducting education meetings before moving participant assets. This can help employees better understand the upcoming overhaul and what they can do afterward to change investment direction. It's also helpful to explain the benefits of target-date funds—then, eligible employees can feel comfortable with the decision the plan is making on their behalf.

For the plan's fiduciaries, the Investment Reset strategy requires the most caution of the three strategies discussed in this brochure. Because there is no "safe harbor" that will automatically shield them from liability, fiduciaries must be prepared to demonstrate that the Investment Reset strategy is prudent and in the best interest of the plan's participants. And, of course, be sure to consult your legal counsel who can help you size up the risk and advise you about the issues you should consider as you analyze this strategy.

* Timing varies by implementation strategy for each plan and recordkeeper—you'll need to take various factors into consideration. It's important to discuss implementation timing and capabilities with your recordkeeper to set proper expectations.

Targeting Better Outcomes

Most participants want help with their retirement investing. How you provide that help makes a big difference.

Finding the Right Fit for Your Plan

"Just do it for me." That's what many plan participants tell us they want. Target-date funds can do just that—but it depends on how you incorporate them into your plan.

- The Add-to-Menu strategy provides access to the benefits of target-date funds. But it won't do much to combat participant inertia—even if you map assets over to the target-date funds when eliminating other investment options. Typical result: less than 2% of assets into target-date funds.
- The Investment Re-election strategy will give your Accidental investors more of the helping hand they need while respecting the independence of your Active investors. Typical result: 50% to 80% of assets into target-date funds.
- The Investment Reset strategy turns participant inertia from an obstacle into an advantage. Typical result: 80% to 95% of assets into target-date funds.

When you enhance your plan, you'll want to make sure your changes are effective—that you've actually connected your participants with the help and solutions they need.

Creating a Connection

Participants generally appreciate target-date funds. In fact, many Active investors "default" to the target-date funds and keep their assets there—not because of inertia, but because they feel it's simply a better solution.

So when you decide on the implementation strategy for your plan, think about the best way to connect your participants with a better route to retirement investing.

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When applying a particular asset allocation model for retirement investing, your participants should consider their other assets, income, and investments (e.g., equity in a home, IRA investments, savings accounts, and interests in other qualified and non-qualified plans) in addition to any investment in your firm's retirement plan.

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