PLAN SPONSORS SPEAK WITH ACTION

The Shift from Recordkeeper Proprietary Target-Date Funds to Nonproprietary Solutions

RESEARCH METHODOLOGY

The data set in this report covers a total of 7,801 401(k) plans with $2.4 trillion in assets and 27.9 million participants in 2015. All data were gathered from Form 5500 and its Schedule of Assets for 401(k) plans with more than 100 participants and $1 million in assets.

The data sample includes all 401(k) plans for which BrightScope has investment lineup information and an assigned recordkeeper for each year from 2009 through 2015. Recordkeepers were assigned to plans based on Form 5500 Schedule C provider codes. If multiple providers were listed, the recordkeeper that receives the highest fee is assumed to be the plan's recordkeeper.

BrightScope re-created this analysis in a similar manner as was done previously, excluding such recordkeepers as State Street, Hartford Financial and Lincoln Financial. For 2015, Empower, Putnam and Great-West are all considered proprietary to one another on all outputs as a result of an October 2014 merger. New York Life funds are proprietary to John Hancock as the result of an April 2015 acquisition.

Because we looked at plans that fit the criteria as of a specific query run date and viewed them over the course of a defined time frame, the plan set may differ slightly from the original report published.

White-label target-date funds are included in the data, and the asset manager may not be apparent, such as in "AT&T Target Retirement 2040."

PROPRIETARY OR NONPROPRIETARY?

When the Pension Protection Act (PPA) was passed in 2006, target-date funds (TDFs) became the default option of choice for plan sponsors. Funds offered by recordkeepers—known as proprietary funds—quickly gained the lion's share of industry assets. Today, the top three target-date providers are asset managers that also provide recordkeeping services.

But the target-date landscape has been changing rapidly, and so have plan sponsors' preferences. Joint research conducted by AllianceBernstein (AB) and BrightScope in 2017 showed that fewer plan sponsors were using their recordkeepers' proprietary TDFs—and that more plan sponsors were choosing nonproprietary TDFs from other managers. The two firms revisited the data for 2015 (the most recent year for which data are available)—data spanning more than 7,800 401(k) plans and representing $2.4 trillion in assets and 27.9 million participants—to see if the trends continued.

WHAT WE FOUND

1. **Recordkeepers' proprietary TDF share has declined by 20% since 2009, as the use of nonproprietary TDFs has increased by 19%. Both of these numbers are up from the last study.**

2. **Large recordkeepers have been hit the hardest: most have lost proprietary TDF share since 2009, and very few have gained share.**

3. **More smaller plans (53%) use recordkeeper proprietary TDFs. Usage among large[1] plans is much lower (31%), because "unbundling" of target-date decisions from plan administration decisions is more common.**

4. **The use of collective investment trusts (CITs) in TDFs has jumped since 2009, with some recordkeepers using CITs or passively managed TDFs to reduce fees and keep their proprietary share.**

1 Small plans are defined as $100 million—$250 million and large plans as $1 billion and higher.

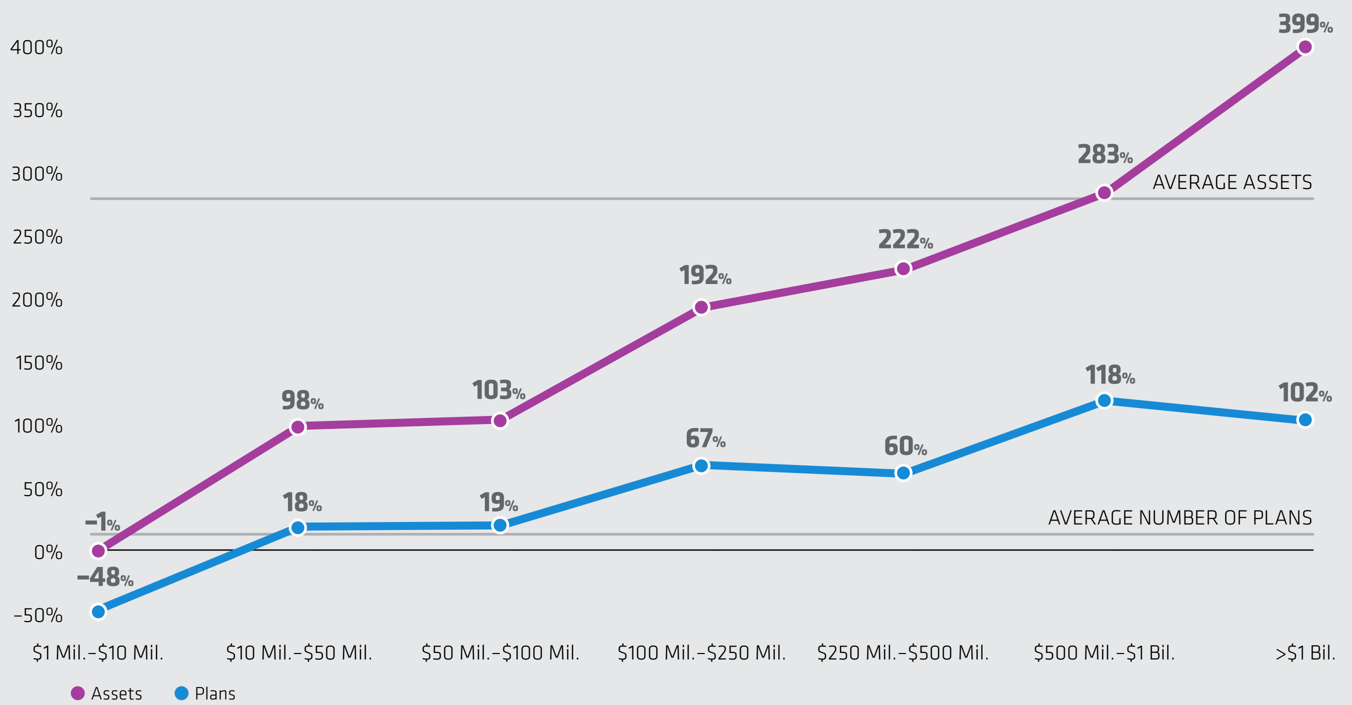
THE TDF MARKET IS EVOLVING

Today's target-date fund market spans more than $1.61 trillion in assets.[2] TDFs are the principal default investment for most 401(k) plans, with our research focusing on approximately 37,500 plans now invested in these solutions. That's nearly 75% of all plans with a publicly available investment menu.[3]

And the growth has been fast. Between 2009 and 2015, the number of plans using TDFs has grown by 17% and assets have grown by 275%, with significant growth in larger plans with more than $500 million in assets. With the market already large and with growth expected to continue, asset managers are positioning themselves for greater share, launching new target-date offerings and enhancing existing ones.

The competition is a lot more crowded today. There are about 51 target-date managers in the market offering more than 108 different TDF series.[4]

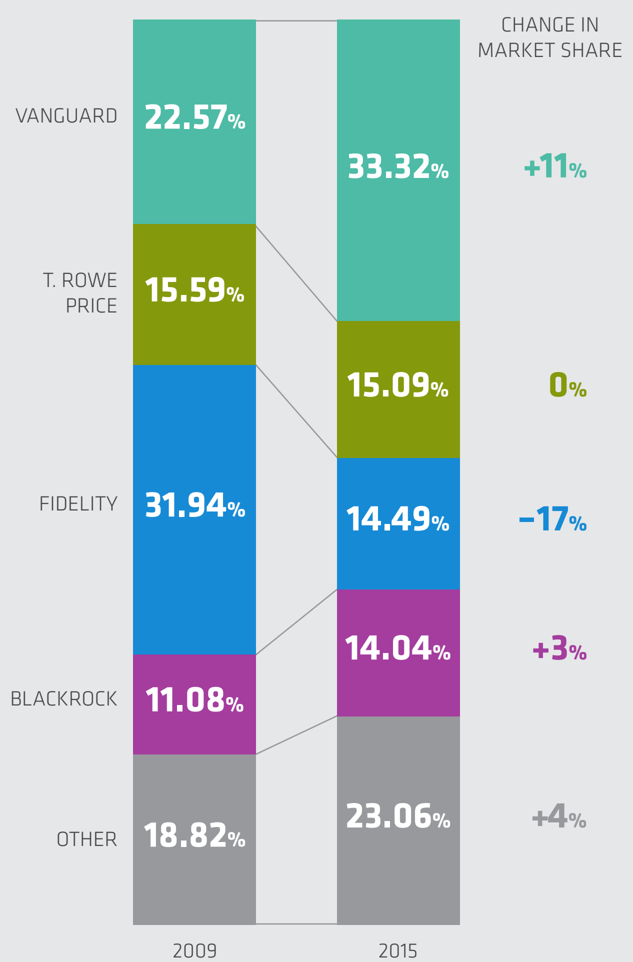
GROWTH FROM 2009 TO 2015 SKEWED TOWARD THE LARGER END OF THE MARKET



Due to the time-series data, a plan may have been in the $10 million–$50 million group in 2009, but as the plan grew over the course of the analysis period, it could have ended up in the $100 million–$500 million group in 2015.

2 Represents target-date mutual fund assets according to Strategic Insight Simfund and CIT assets according to BrightScope
3 The total number of plans within BrightScope's system is significantly higher.
4 Includes mutual funds, CITs and insurance company group annuity series

FOUR TARGET-DATE MANAGERS DOMINATE NEARLY 77% MARKET SHARE OF THE ASSETS



But four managers still dominate the market today: nearly 77% of assets are held by Vanguard, T. Rowe Price, Fidelity and BlackRock. That leaves 47 other managers fighting for what's left.

How did these "big four" get such a commanding position? A little history sheds some light. When the PPA was passed in 2006, most plan sponsors chose their qualified default investment alternative (QDIA), usually a TDF, by simply adding their recordkeeper's target-date offering. Many recordkeepers offer a discount on their services if sponsors select their TDF, making it even easier for plans to select proprietary offerings.

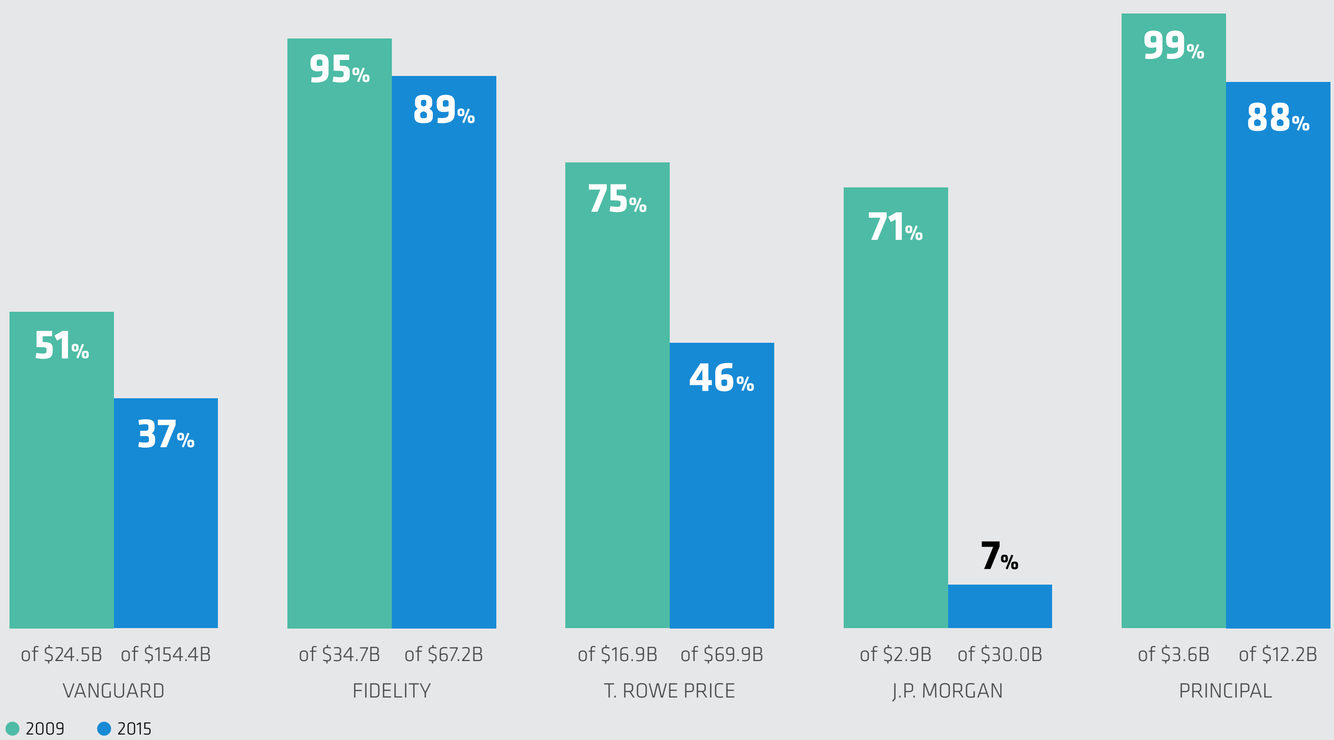
TARGET-DATE MANAGERS FARE BEST WHEN LESS RELIANT ON THEIR OWN PLATFORMS.

But things are changing for proprietary target-date providers. Simply put, they're finding it harder to maintain share of target-date assets on their own platforms, as plan sponsors continue to unbundle their target-date fund and recordkeeper decisions. Many plan sponsors now choose TDFs from outside managers.

The proprietary target-date managers who are faring the best have made themselves less dependent on their own recordkeeping platforms. Instead, they've focused on placing their TDFs on other recordkeepers' platforms, broadening distribution. Vanguard and T. Rowe Price, for example, had a much lower percentage of target-date assets on their own recordkeeping platforms in 2015 compared with 2009. Managers like Fidelity and Principal Financial Group, on the other hand, still depend a lot on target-date assets from their recordkeeping clients. The significant difference for J.P. Morgan is attributable to Empower's acquisition of J.P. Morgan's recordkeeping business in 2014.

THE ASSET MANAGER VIEW: LARGE TDF MANAGERS ARE NO LONGER DEPENDENT ON THEIR OWN RECORDKEEPING PLATFORMS

Proprietary TDF Assets on Their Own Platform (Percent)



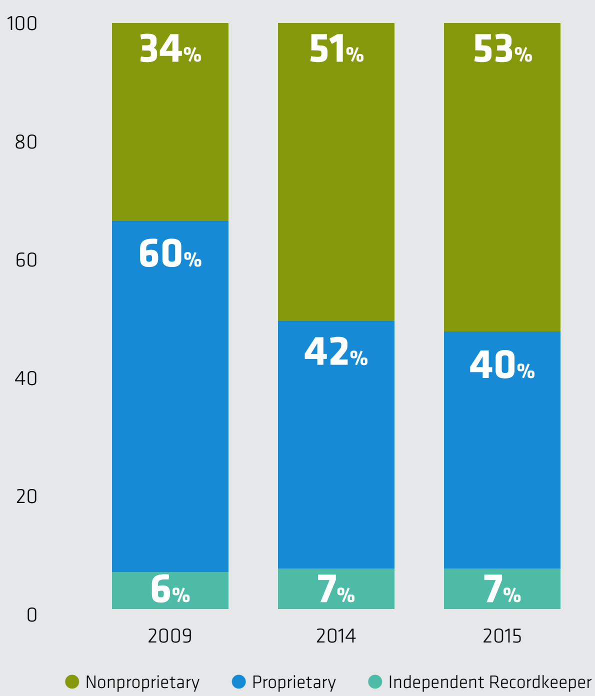
PROPRIETARY TDFs CONTINUE TO LOSE GRIP ON THEIR OWN PLATFORMS

The shift in proprietary TDFs is evident from the changing composition of recordkeepers' target-date assets from 2009 to 2015.

As a percentage of recordkeepers' target-date assets, proprietary fund share has tumbled from 60% to 40% from 2009 to 2015. On the other hand, the share of nonproprietary TDFs on platforms leapt from 34% to 53%. Compared to 2014, this shift seems to be moving in the same direction. Target-date assets on the platforms of recordkeepers that don't offer their own TDFs—such as Ascensus and ADP—have remained about flat. Clearly, nonproprietary target-date solutions are continuing to gain steam.

THE RECORDKEEPER VIEW: USE OF RECORDKEEPERS' PROPRIETARY TDFs CONTINUES TO DECLINE

Recordkeepers' Target-Date Assets (Percent)



With more choices than ever before, many plan sponsors are decoupling their choice of recordkeeper from their target-date-solution choice.

LARGE PLANS ARE AHEAD IN THE SHIFT TO NONPROPRIETARY

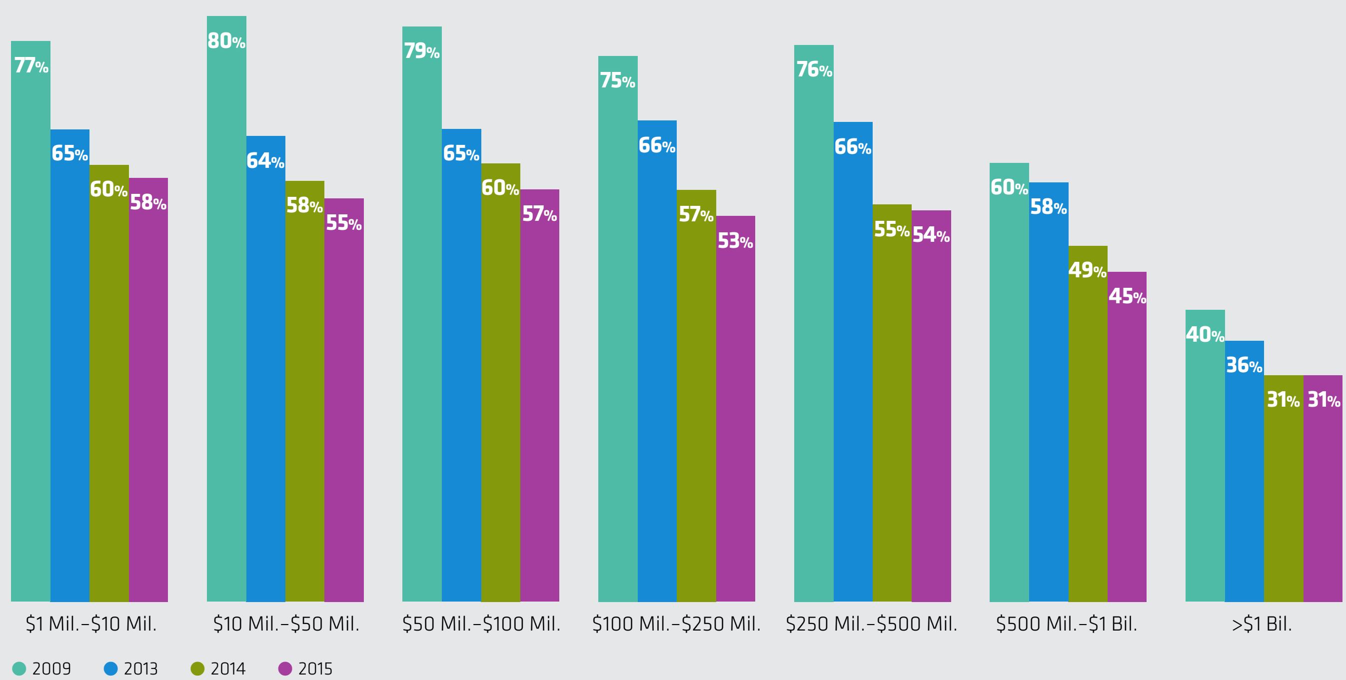
The use of proprietary TDFs has declined for plans of all sizes, but there are distinctions when we break the numbers down by plan size.

In the largest plans with more than $1 billion in assets, the penetration of proprietary TDFs was the lowest at 31% in 2015. That's down from 40% in 2009 and 36% in 2013—just after the US Department of Labor's Tips for ERISA Plan Fiduciaries on target-date selection were published. These tips encouraged plan sponsors to consider nonproprietary and custom funds. But it's not likely that plan sponsors reacted to the DOL tips so quickly that they moved away from proprietary funds by 2015. However, the data continue to show that plan sponsors are slowly moving in that direction.

Regardless, many large plans have already unbundled their target-date and recordkeeper decisions. On the other side of the coin, more than 55% of smaller plans with less than $100 million in assets still use proprietary TDFs.

PROPRIETARY TDF ASSETS ON RECORDKEEPER PLATFORMS HAVE DECREASED IN ALL PLAN SEGMENTS

Assets by Plan Size (Percent)



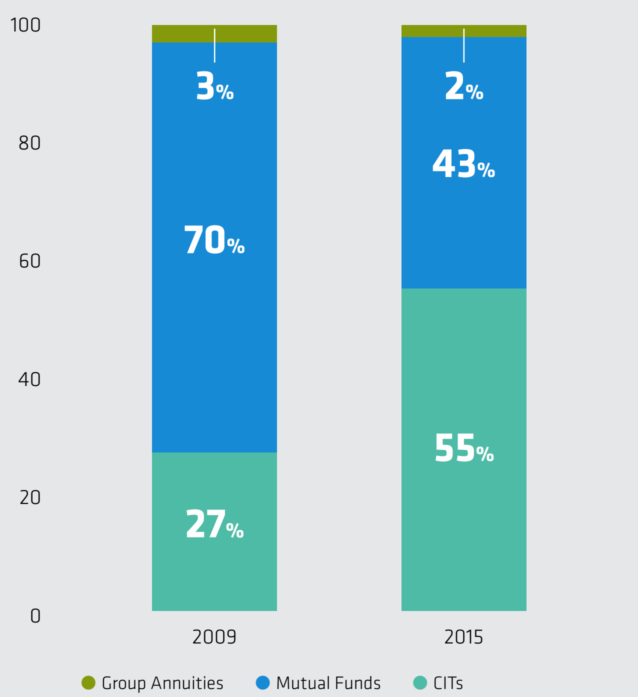
CITs GENERALLY COST LESS THAN MUTUAL FUNDS, MAKING THEM MORE ATTRACTIVE TO PLAN SPONSORS.

MORE PLANS ARE CHOOSING COLLECTIVE INVESTMENT TRUSTS

CITs have been gaining traction in DC plans, primarily as a way to help reduce costs, which is a continued focus for plan sponsors in the current regulatory and litigious environment.

From 2009 to 2015, the use of target-date collective investment trusts more than doubled as a percentage of target-date assets, from 27% to 55%. This growth came at the expense of target-date mutual funds, which saw their usage fall from 70% to 43% over the same period. This is consistent with much industry research that documents the shift to CITs across all defined contribution (DC) assets. Large plans have led the way in CIT adoption, but smaller and midsize plans are stepping in as providers begin to make these vehicles more accessible by reducing minimum required investments.

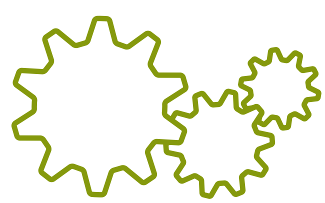
THE USE OF TARGET-DATE CITs IS GROWING RAPIDLY
Target-Date Assets by Vehicle (Percent)



WHAT ARE THE POTENTIAL BENEFITS OF CITs?

1. Low Cost and Transparency

2. Efficiency of Operation



3. Easy Access to Information

WHICH RECORDKEEPERS ARE—AND AREN'T—GETTING THEIR SHARE?

The footprint of proprietary TDFs on recordkeepers' own platforms is generally shrinking, but the trend isn't uniform. In fact, proprietary TDF share as a percentage of both plans and assets on any given platform varies widely.

On the left side of the display below, we rank recordkeepers according to the percentage of plans on their platforms that use the proprietary TDF. On the right, we rank recordkeepers by the percentage of plan assets on their platforms that are in proprietary TDFs.

American Funds tops both lists. Of the plans on its platform, 98% use American Funds' proprietary target-date series. And nearly all of the target-date assets on American Funds' platform are in the proprietary offering.

For Vanguard, there's a slight disparity in the two numbers: 98% of the plans on its recordkeeping platform are in proprietary TDFs, but only 93% of the target-date assets on the platform are. It may be that Vanguard's larger plans want Vanguard as their recordkeeper but have chosen to use another manager's TDFs.

Fidelity is another such example, with a much bigger split: 63% of plans on its recordkeeping system use proprietary Fidelity TDFs, but only 33% of the target-date assets are invested in these proprietary funds.

RECORDKEEPERS WITH HIGHEST PROPRIETARY TDF SHARE (2015)

Plans with Proprietary TDFs		Proprietary TDF Assets	
Recordkeeper	Percent of Plans	Recordkeeper	Percent of Assets
American Funds (Capital Group)	98	American Funds (Capital Group)	99
Vanguard Group	98	T. Rowe Price	94
T. Rowe Price	94	Vanguard Group	93
Principal Financial Group	84	Principal Financial Group	75
J.P. Morgan	73	J.P. Morgan	61
TIAA-Nuveen	64	Charles Schwab	46
Fidelity	63	TIAA-Nuveen	33
John Hancock*	49	Fidelity	33
Charles Schwab	46	Bank of Oklahoma	26
Wells Fargo	33	Prudential Financial	22
Prudential Financial	29	BMO Harris Bank	20
BMO Harris Bank	26	Wells Fargo	15
Bank of Oklahoma	25	John Hancock*	13
Voya Financial (ING)	23	MassMutual	13
Nationwide Mutual Insurance	23	Nationwide Mutual Insurance	11
MassMutual	16	Empower	2
Empower	11	Voya Financial (ING)	1
Transamerica	3	Transamerica	0

***** John Hancock data reflect the 2015 acquisition of New York Life.

BOTTOM LINE: MOST RECORDKEEPERS HAVE LOST PROPRIETARY SHARE

Although the numbers vary considerably among recordkeepers, since 2009 only two of them were able to increase their share of proprietary target-date assets.

J.P. Morgan falls above the diagonal line, which indicates that it gained proprietary assets over the six-year period. The majority of recordkeepers fall either on or below the line; they've remained flat or lost share in proprietary assets since 2009.

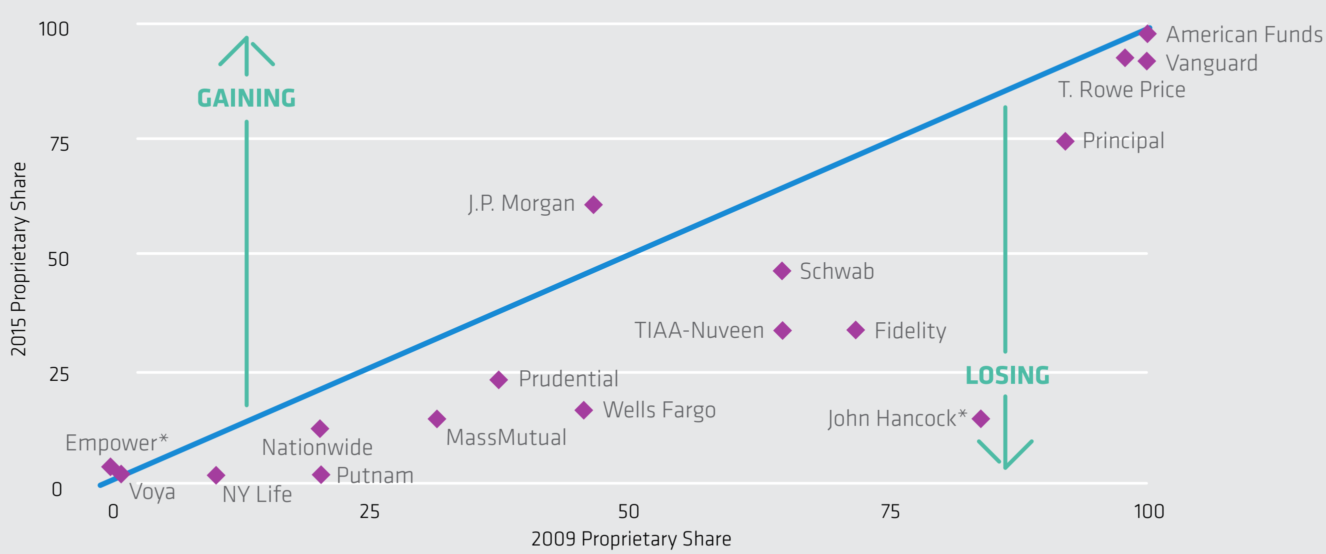
Keep in mind that a lot of change and consolidation continues to take place among recordkeepers; that needs to be considered when looking at the data.

Great-West Financial acquired J.P. Morgan's Retirement Plan Services recordkeeping unit in October 2014, which ultimately became Empower Retirement. This was one of the largest acquisitions in the industry and it resulted in what is the second largest recordkeeper today.[5] Taking this acquisition into account, Empower has seen its share of proprietary target-date fund assets increase very modestly. Conversely, we saw a dip in John Hancock's share of proprietary target-date fund assets following its acquisition of New York Life in 2015.

Fidelity, as noted earlier, has seen a significant drop in the asset share of its proprietary offerings. In 2009, 72% of the target-date assets on its recordkeeping platform were in Fidelity TDFs. That number fell to only 33% in 2015. The trend has been fairly consistent across all plan sizes, but it's a bit more pronounced in larger plans.

LARGE RECORDKEEPERS ARE LOSING PROPRIETARY SHARE

Proprietary Share of Assets in 2009 and 2015 (Percent)



* 2009 data for Empower are representative of Great-West assets. 2015 data for John Hancock reflect the 2015 acquisition of New York Life.

5 Based on total DC plan participants

DOL TIP: “INQUIRE ABOUT WHETHER A CUSTOM OR NONPROPRIETARY TDF WOULD BE A BETTER FIT FOR YOUR PLAN.”

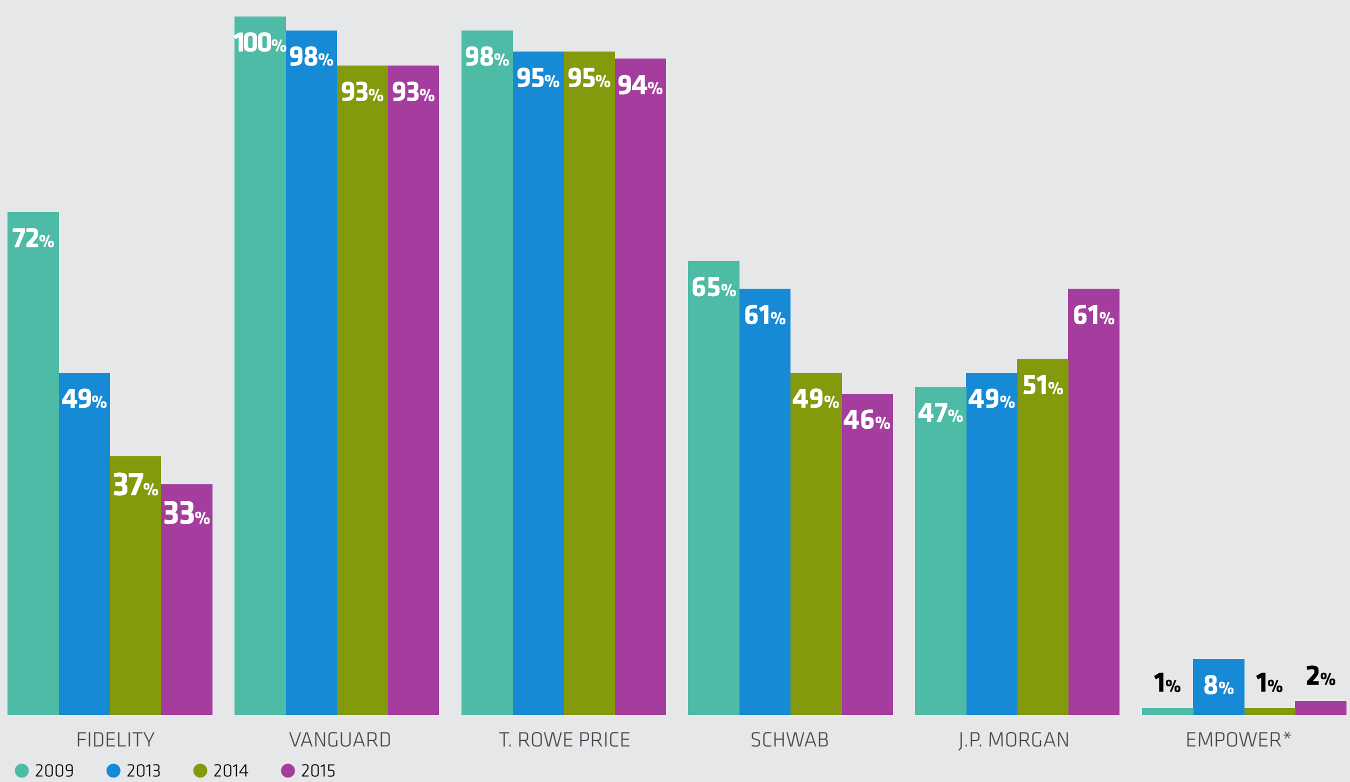
WHAT IMPACT HAVE THE DOL TIPS MADE SO FAR?

As we mentioned earlier, we wanted to find out if the 2013 DOL Tips for ERISA Plan Fiduciaries, which encourage plan sponsors to consider nonproprietary or custom funds, made an impact on the nonproprietary migration we've seen.

The data show a decrease in proprietary target-date asset share for some top recordkeepers between 2013 and 2015, but it's likely too soon to say whether the DOL tips affected—or will affect—target-date choices. Recordkeepers like Fidelity and Schwab have been losing proprietary share since 2009, but Vanguard and T. Rowe Price have seen only modest shifts. In fact, they've generally been able to hang on to most of their share.

PROPRIETARY TARGET-DATE SHARE FOR TOP RECORDKEEPERS

Proprietary Share of Assets (Percent)



* 2009–2014 data for Empower are representative of Great-West assets.

WHAT'S A RECORDKEEPER TO DO?

What have recordkeepers done to try to keep their proprietary target-date share? The data suggest that some recordkeepers have introduced a target-date series in a CIT or passively managed format.

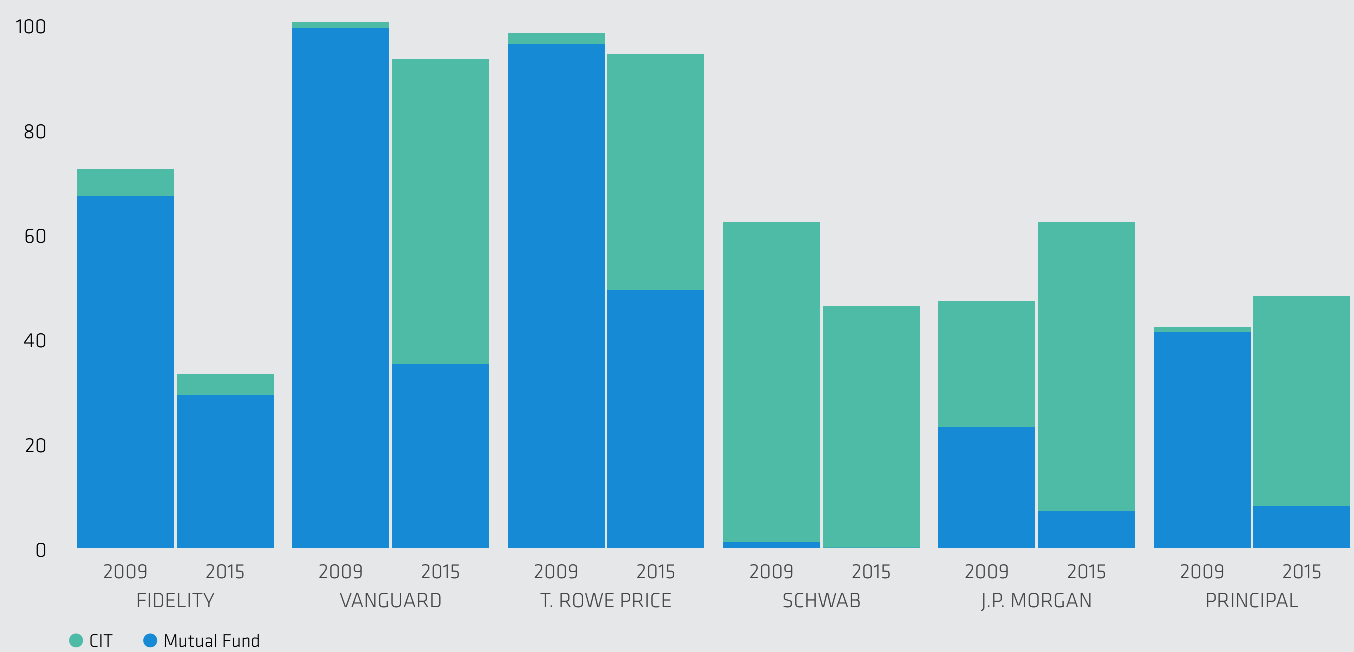
CITs generally cost less than mutual funds, making them more attractive to plan sponsors. This could indicate a move by recordkeepers to keep their business with a plan sponsor who might want to shift to another manager's lower-cost target-date series.

Take Vanguard, for example. In 2009, nearly all the target-date assets on its platform were invested in Vanguard target-date mutual funds. By 2015, 58% of the assets were in Vanguard's target-date CIT series and only 35% in its mutual fund series. The data show a similar shift for T. Rowe Price: 96% of its target-date assets were in the firm's target-date mutual fund series in 2009, but by 2015, only 49% were in the mutual fund series, with 45% in the CIT series. This is a significant transition in a relatively short time.

Some recordkeepers may have taken a different approach to hold on to their proprietary shares: introducing a passively managed target-date series. In 2009, 6% of Fidelity's proprietary share of target-date assets were in its passively managed target-date series. But by 2015, that share had more than doubled to 13%. Schwab's proprietary share was 100% actively managed in 2009. The firm

CERTAIN RECORDKEEPERS HAVE USED CITs TO HOLD PROPRIETARY SHARE...

Proprietary Share of Assets by Vehicle (Percent)

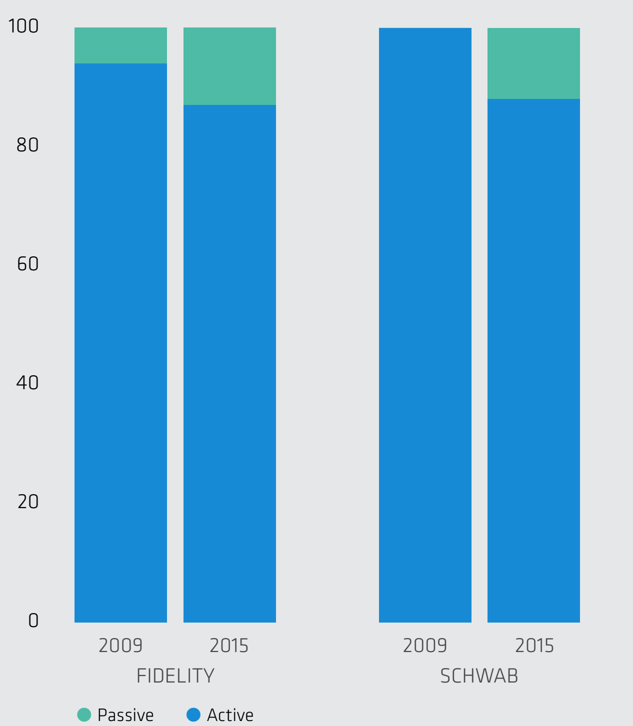


introduced a passively managed CIT series in 2009, and by 2015 it accounted for 12% of Schwab's proprietary share.

Today, many target-date providers are doing even more to hold their ground and compete for new business by reducing fees and expenses. How will these strategies impact the proprietary share? That will be something to examine in future research.

...AND SOME HAVE RELIED ON PASSIVE TDFs TO RETAIN PROPRIETARY SHARE

Proprietary Share in Active and Passive TDFs (Percent)



MYTH

It's complicated to educate participants about CITs, and participants can't easily get pricing or performance information.

FACT

Many CITs are simply clones of mutual funds. Every plan must disclose information about the product type, but the vast majority of participants won't care about the legal technicalities that distinguish them. In fact, CITs look the same as mutual funds to participants.

WILL SMALLER PLANS FOLLOW THE TREND?

In terms of keeping proprietary target-date share, recordkeepers have been more successful with smaller plans—with a few exceptions (these may be caused by a few larger plans distorting the data for those recordkeepers' larger plan segments).

Many larger plan sponsors have already separated the recordkeeping and target-date decisions, evaluating each on its own merit. In many cases, the recordkeeper's TDF may be a strong choice. But generally, smaller plans haven't yet moved away from using their recordkeepers' proprietary TDF to the extent larger plans have. It remains to be seen whether smaller and midsize plans will follow suit over time, but the greater scrutiny on fiduciary decision-making may influence these decisions.

WHAT DOES THE FUTURE HOLD FOR TDFs?

The target-date marketplace continues to change, with growing emphasis on the fiduciary role of plan sponsors, consultants and advisors.

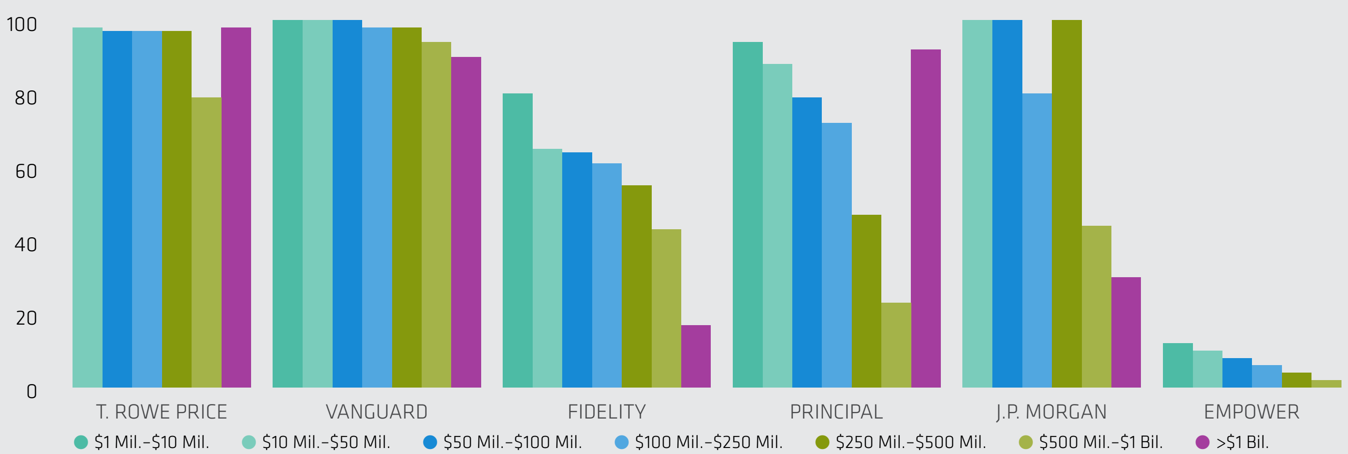
Will decision-makers for plans of all sizes continue to look more carefully at their target-date decisions? Will recordkeepers face tougher challenges in trying to keep market share in their own TDFs on their platforms? Will the DOL tips have more of an impact on target-date selection as we look at 2016 plan data and beyond?

The jury is still out on many of these questions, pending the availability of newer data, but the numbers in hand clearly show a shift toward nonproprietary TDF offerings. The competition is stiff, with more and more asset managers offering TDFs—and the battle seems likely only to intensify.

With more choices than ever before, many plan sponsors are decoupling their choice of recordkeeper from their target-date-solution choice. Plan sponsors are seeking the best possible outcomes for plan participants—by keeping them on a path toward being more financially prepared for retirement. Better-quality portfolio management, lower fees and solid investment performance all help—and plan sponsors are now looking at a broader set of options before making a decision.

PROPRIETARY TARGET-DATE SHARE IS SIGNIFICANTLY HIGHER FOR SMALLER PLANS

Proprietary Share of Assets by Plan Size: 2015 (Percent)



PROPRIETARY TDF ASSETS BY RECORDKEEPER

Plans with Proprietary TDFs

Recordkeeper	2009 Proprietary Assets ($)	2015 Proprietary Assets ($)
Fidelity	32,720,678,837	57,540,666,573
Vanguard Group	12,299,108,097	56,165,838,918
T. Rowe Price	12,245,336,705	31,862,208,821
Principal Financial Group	3,566,382,396	10,401,903,847
Charles Schwab	1,544,754,442	5,040,632,643
Wells Fargo	1,198,555,638	2,150,869,010
J.P. Morgan	2,029,290,651	1,315,009,919
TIAA-Nuveen	99,520,008	830,435,456
American Funds (Capital Group)	147,261,280	612,452,979
Prudential Financial	255,205,280	505,722,301
John Hancock*	122,379,120	498,217,484
MassMutual	353,223,673	462,968,784
Empower*	1,465,455	397,369,375
BMO Harris Bank	66,361,887	200,172,425
Bank of Oklahoma	33,382,136	99,518,330
Voya Financial (ING)	117,541,440	76,466,364
Nationwide Mutual Insurance	10,189,996	17,169,111
Mutual of America	–	11,098,900
Transamerica	–	7,628,030
New York Life	90,409,887	–

* 2009 data for Empower are representative of Great-West assets. 2015 data for John Hancock reflect the 2015 acquisition of New York Life.

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