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The Path Forward

DC Participants Want More

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THE PATH FORWARD

DC PARTICIPANTS WANT MORE

May 2015

Defined contribution (DC) plans now are the primary retirement savings vehicle for U.S. employees. With $6.8 trillion in assets as of December 31, 2014,[1] and more than 88 million total participants,[2] DC plans are the only type of employer-sponsored retirement vehicle accessible to many younger workers in the private sector. So it only makes sense that these plans should work as effectively as possible for all workers.

Today, employer-sponsored defined benefit (DB) pension plans, which had formed the foundation for employee retirement funding since World War II, are increasingly rare. Just 30 Fortune 100 companies offered a DB plan to newly hired salaried workers in 2013, and the large majority of these were hybrid DB plans.[3] Unlike traditional DB plans, hybrid plans define the accrued benefit, or a portion of the accrued benefit, in the form of a hypothetical account balance or accumulated percentage of final average compensation. They are often paid as lump sums upon termination of employment rather than as monthly income in retirement.

Even current beneficiaries of DB plans have reason for concern as private-sector companies seek to limit their exposure to pension risk and as public-sector plans struggle with unfunded liabilities. As for the U.S. Social Security system, the reluctance of political leadership to address the program's funding crisis may put easier fixes out of reach, possibly resulting in reduced benefits for future retired American workers.

Because DC plans will play such a critical role in the retirement security of American workers, they must be as effective as possible in helping participants accumulate enough assets to enter retirement on a secure basis. While there are numerous reasons DC plans continue to fall short of participants' needs, many are rooted in the fact that DC plan participation is largely voluntary. It is the participant who decides whether to enroll or opt-out, how much to contribute, how to invest his or her contributions and when to withdraw the money. Thus, the most effective DC plans must use plan design or education to persuade all employees, whether hourly workers or highly compensated executives, to participate at a level that can help ensure their financial security in retirement.

To better understand the driving factors behind these problems, we interviewed DC plan consultants, plan sponsors and plan participants over the course of five months. In the end, we've identified five key strategies to help address these systemic challenges. (See page 13 for more information about our study process.)

FIVE WAYS TO HELP EMPLOYEES

While some companies may offer a DC plan to maintain a competitive advantage, we believe it is likely that most plan sponsors provide a DC plan because they genuinely want to improve their employees' financial security in retirement. The fifth edition of *The Path Forward*, Northern Trust's DC plan research series, provides direction toward that objective through these five recommendations:

1. **Step It Up —** Increase the employer role in encouraging retirement savings by taking a stand on how much different groups of employees (grouped by salary level or age) should save for retirement and encouraging participation in retirement planning.
2. **Set Auto Features at Meaningful Levels —** Improve automated plan design features by auto-enrolling at a 6% deferral rate and allowing auto-escalation to more than 10% of salary.
3. **Provide Projections —** Add projections to account statements to provide participants with retirement planning information beyond their current account balance.
4. **Streamline Your Menu —** Simplify the investment menu by reducing the number of investment options in the line-up and using easier-to-understand descriptors of each investment.
5. **Introduce In-Retirement Choices —** Add investment options specifically designed for retirees that provide a stream of predictable income.

By implementing these recommendations, we believe plan sponsors can help improve the DC retirement system and create a more-secure retirement for American workers.

INCREASING THE EMPLOYER ROLE

Simply providing participants with a DC plan and retirement planning tools is not sufficient to ensure they will adequately plan and save for retirement. The median percentage of salary deferred to a DC plan is just 6%, according to *The Path Forward* survey of plan participants. Three in 10 (29%) contributed up to the level of the match but no more, while one in 10 (9%) contributed less than the match. Almost four in 10 (38%) plan participants reported they are not confident that they know how much they need to save each year to have a financially secure retirement, and another 42% are only somewhat confident. They likely are correct. According to the Employee Benefit Research Institute (EBRI) 2014 Retirement Confidence survey, half (52%) of American workers with a retirement plan have less than $50,000 in total savings and investments.[4] While there is no industry consensus about the "right" amount to save, many experts recommend deferring 10% to 15% of salary even for those who begin contributing at age 20.[5] Workers who start saving later in their career need higher deferral levels.

To help address this savings gap, employers should play a larger role in encouraging retirement savings. They can take a position on the amount that different groups of employees (grouped by salary level or age group) should save for retirement and encourage participation in retirement planning. This effort could include messages from senior management identifying desirable retirement savings levels, making meeting space available for retirement planning sessions and giving employees time to attend meetings or webinars.

The recent *The Path Forward* survey of plan participants suggests that they would welcome, rather than resent, encouragement from their employer and recommendations on how much to save. (See Figure 1.) More than seven in 10 (72%) favor employers providing a viewpoint to all employees on contribution amounts. Perhaps more telling, plan participants are unlikely to simply dismiss employer recommendations on how much to save. More than eight in 10 (84%) state that if their employer provided advice about how much employees should contribute to the 401(k) plan, they would either adopt the advice or consider it when deciding how much to contribute. (Figure 2, page 4.) Among those with personal income of less than $30,000, 88% say they would consider the employer's advice.

Eight in 10 plan participants strongly or somewhat favor employers encouraging employees to contribute to their 401(k) plan.

FIGURE 1: PARTICIPANT REACTIONS TO TYPES OF EMPLOYER ENCOURAGEMENT

Would you favor or oppose your employer doing each of the following as part of the 401(k) plan?

Total (n=1,007)

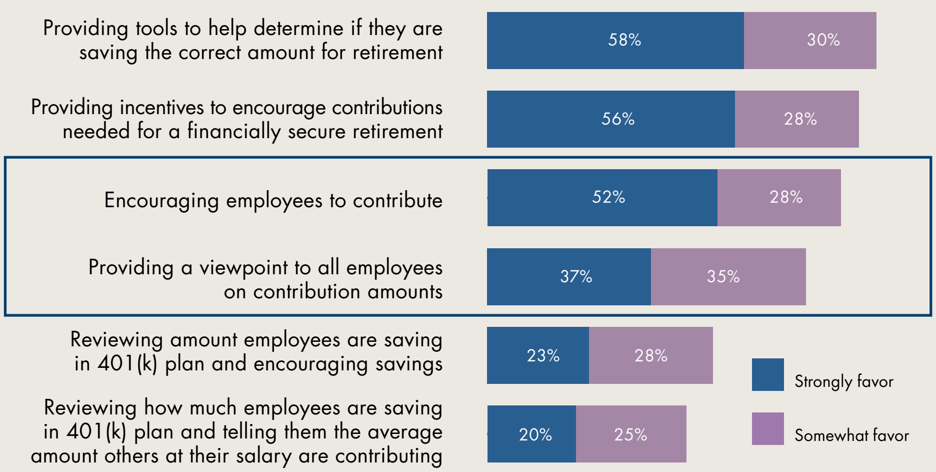
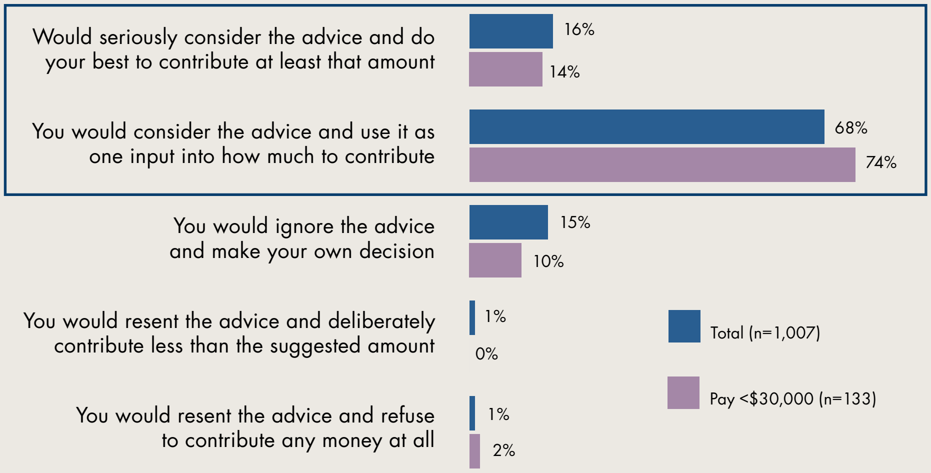


FIGURE 2: PARTICIPANT REACTION TO EMPLOYER ADVICE ON CONTRIBUTION

If your employer provided advice about how much you and other employees should contribute to the 401(k) plan, which one of the following comes closest to what you think your reaction would be?



Plan sponsors interviewed for *The Path Forward* generally agree about the desirability of allowing plan participants time off to attend meetings about the plan, offering interactive webinars and sending general messages encouraging retirement savings. They have real concerns, however, about providing participants with targeted recommendations – by salary level or age – about how much they should be saving. Many believe the idea is worth discussing if it fits the corporate culture and philosophy but think management's role as a fiduciary must be clarified before senior leaders would be comfortable providing specific savings recommendations.

While Northern Trust is not aware of anything in the Department of Labor's (DOL) regulations that suggests specific savings recommendations pegged to salary level or age would be a fiduciary concern, it is clear many of the plan sponsors we interviewed share this concern. As such, we believe these concerns must be addressed by the DOL before some plan sponsors will be comfortable making such recommendations. In the meantime, we believe concerned plan sponsors should consider providing report cards to individual participants that challenge them to assess their situation and make changes to their spending and saving.

The financial resource constraints of lower-income or younger employees is a secondary concern making some of the plan sponsors surveyed reluctant to offer specific savings recommendations. It is notable, however, that lower-income participants do not share these same concerns. An employer-provided recommendation on how much to save simply would be another input to help them decide how much to contribute to their 401(k) plan and would encourage them to save an adequate amount. Plan sponsors sensitive to this issue might consider broadening their strategy to encompass overall financial wellness rather than focusing solely on retirement savings. They may feel that lower-income and younger employees will be more apt to engage based on this more-holistic approach.

"I think there's a lot of liability and sensitivity around senior management's involvement in the savings plan and seeing that as something endorsed by senior management. ... Fiduciary concerns are always present and top-of-mind for plan sponsors these days."

Plan Sponsor

IMPROVING AUTOMATED PLAN DESIGN FEATURES

According to recent industry surveys, half (50%) of plan sponsors now include auto-enrollment in their plan, with most (60%) setting the automatic deferral level at 3% or less.[6] By starting so low, however, employers unintentionally are providing inadequate guidance to employees on how much they should save. In addition, only one-quarter (28%) of plan sponsors include opt-out auto-escalation as part of their plan design. Since most plan participants must save at least 10% of their salary to achieve a financially secure retirement, we believe plan sponsors should auto-enroll at 6% or even higher and allow opt-out auto-escalation of deferral rates to more than 10%.

The Path Forward survey of plan participants suggests that even lower-income plan participants would let their contribution stand (at least at some level) if auto-enrolled at 6% and would let their contributions continue to escalate to 10% or more. If participants who are not currently contributing to their 401(k) plan were auto-enrolled at 6%, just two in 10 (19%) would be likely to cancel their contribution altogether. (Figure 3.) In addition, one-third (32%) would be likely and another 38% would be somewhat likely to let auto-escalation of their contributions stand. (Figure 4.)

> *"I think auto-enrolled and auto-escalation are almost 'musts' — I'm surprised when companies don't have these."*
>
> *Plan Sponsor*

FIGURE 3: PARTICIPANT LIKELIHOOD OF CANCELLING AUTO-ENROLLMENT AT 6% ALTOGETHER

Suppose your employer automatically enrolled you into the 401(k), deducting 6% of your pre-tax salary from your paycheck and putting it into your account in the 401(k) but giving you the option to cancel, decrease, or increase the size of your contribution whenever you want. How likely do you think you would be to cancel the 401(k) contribution altogether?

Participants not currently contributing to a 401(k) plan (n=57)

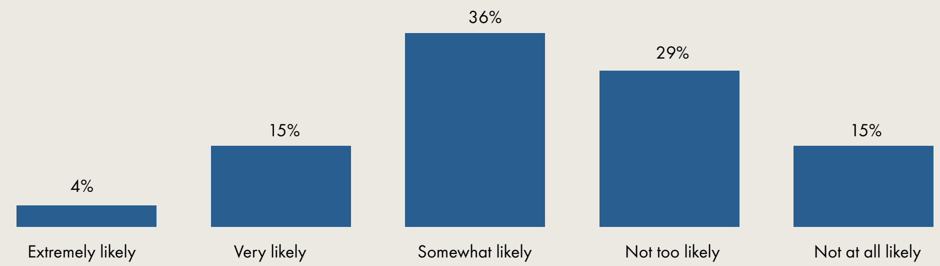


FIGURE 4: PARTICIPANT LIKELIHOOD OF ALLOWING AUTO-ESCALATION TO STAND

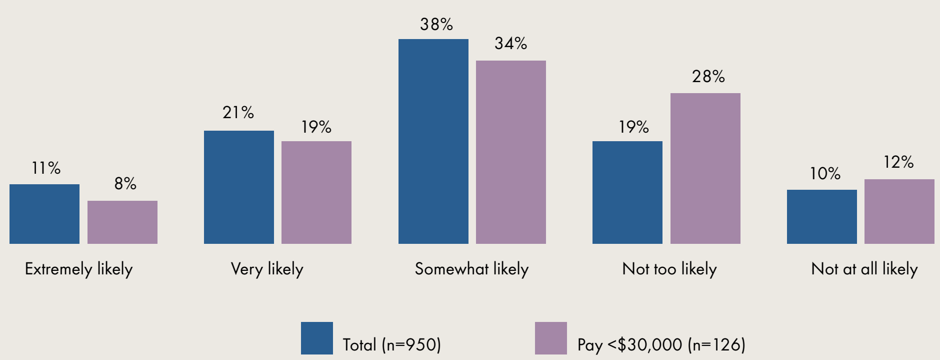
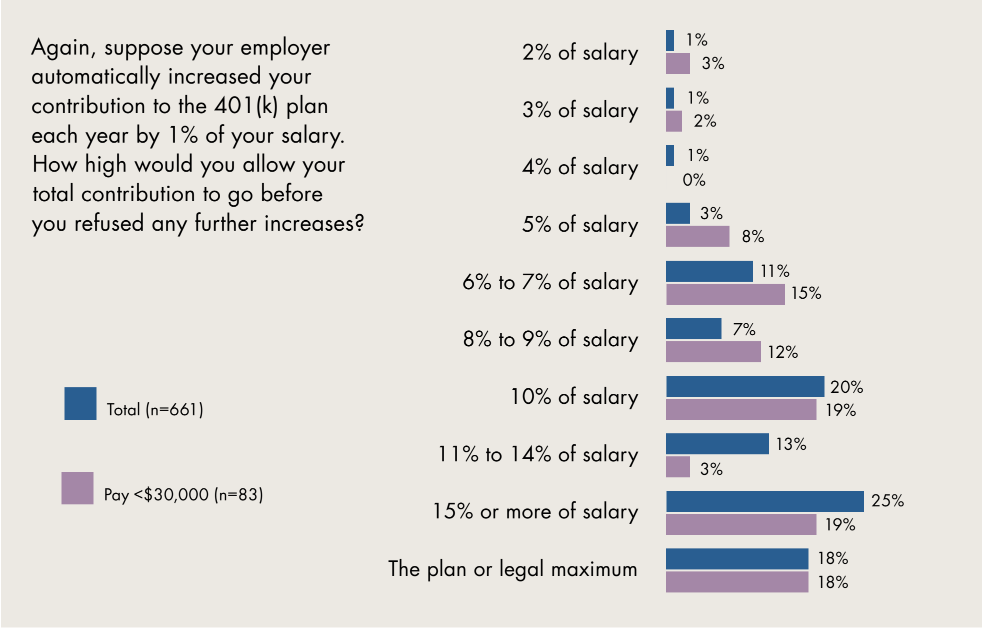


FIGURE 5: PERCENTAGE AT WHICH PARTICIPANTS WOULD REFUSE FURTHER INCREASES IN AUTO-ESCALATION ALTOGETHER



Among these, 43% would let the increases continue to 15% or higher, including 37% of those with personal income of less than $30,000. (Figure 5.)

Despite strong participant and plan consultant buy-in to these DC plan design features, some of the plan sponsors interviewed are reluctant to adopt the more-aggressive targets for auto-enrollment and auto-escalation. They recognize that automatic design features have a much greater impact than communications. Higher targets would push participants who are currently pegging their deferral level to the employer match beyond that plateau. Nevertheless, some of those interviewed believe in auto-escalating to the match but not beyond. These plan sponsors tend to think the suggested percentages are too aggressive.

Many plan sponsors interviewed currently auto-enroll at 3% and auto-escalate to the 5% to 6% level. However, some have implemented these automatic programs for new hires only. It is strongly encouraged, with little apparent downside, to implement these automatic programs at the recommended targets for all plan participants. There would be a one-time administrative cost to implement these changes, but this cost could be minimized if implemented in conjunction with other changes. We also believe that employers should strongly consider conducting periodic re-enrollments of non-participants. While some of those re-enrolled will opt out, the majority appear likely to remain even if at a level lower than the re-enrollment percentage of salary.

A number of plan sponsors interviewed for this research cite one further obstacle to implementing these features: they are not needed to stay competitive. These sponsors feel that the match is more important. Others disagree, saying these automatic features are a competitive requirement, especially for their salaried workforce. Regardless of whether it is a competitive requirement, we believe there is no question that these features would help address chronic under-saving and should be the default in DC plans.

"We currently auto-enroll at 3%, but with proper education of participants, I don't think it would be that difficult to move that 3% to 6%."

Plan Sponsor

ADDING PROJECTIONS TO ACCOUNT STATEMENTS

To help address inadequate retirement planning and goal-setting, employers should ask their plan providers to improve statements by adding projections. These could include indicators about whether participants are on track to save enough for retirement, estimates of how much money participants will have when they retire and calculations of monthly income. They also could provide estimates of amounts needed in order to replace different percentages of income in retirement as well as suggested savings amounts. Offering age-specific projections of how additional contributions would increase retirement income has been shown to increase retirement savings.[7]

We believe account statements should be as effective as possible, since they are the one retirement planning document that every plan participant receives. *The Path Forward* survey results suggest that plan participants consider projections to be important components of an account statement. In addition to their account balance, most plan participants think it is important for the ideal statement to have an estimate of how much money they will have when they retire (79%) and a calculation of the amount of monthly income their projected account balance will produce in retirement (76%). They also want a calculation of the amount of monthly income their retirement savings goal will provide (77%) and a calculation of how many inflation-adjusted dollars they will need for retirement (75%). (See Figure 6.)

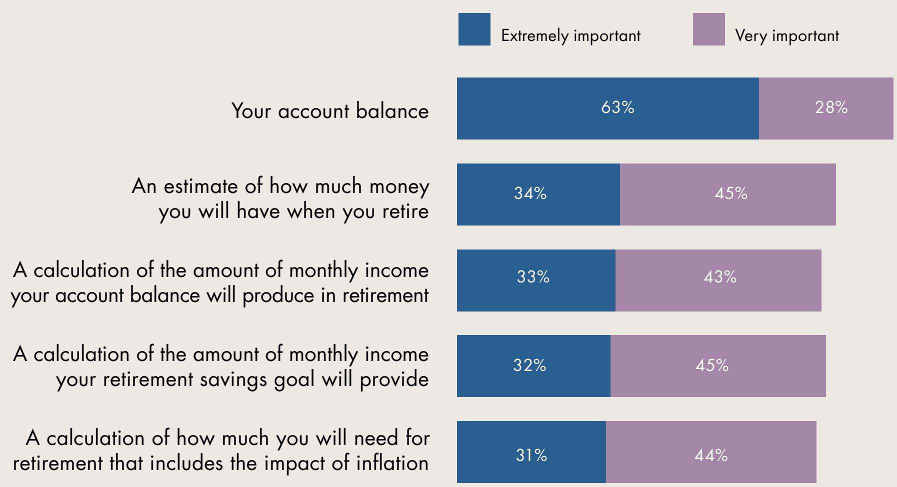
"Trying to provide a picture for participants to understand where they are at and what they might do to improve that picture is an important part of improving outcomes."

Plan Sponsor

FIGURE 6: IMPORTANT ELEMENTS OF ACCOUNT STATEMENTS

Suppose you had the opportunity to design the ideal statement for your 401(k) plan.
How important would it be to include each of the following?

Total (n=1,007)



Most plan sponsors and plan consultants interviewed for this research think putting projections on statements is a good idea because it draws attention to where participants are on the path to saving for retirement. Projections can be a wake-up call for those behind schedule, as 60% of participants in *The Path Forward* survey think they are behind. Projections also potentially can motivate participants to act. Some sponsors and consultants also feel that projected monthly or yearly income in retirement is more meaningful to participants than projecting a lump sum at retirement.

The plan sponsors we spoke with who dislike projections are primarily troubled by the assumptions underlying the projections and the fact that they do not include all household assets. They also contend that projections will go unheeded because not all participants read their statements, though some feel that older participants are much more likely than younger participants to review their statements. These concerns are also on the minds of many who support the projections.

As always, concerns about fiduciary risk and lack of clarity in the DOL regulations are ever-present in the minds of the plan sponsors interviewed. But for most, these concerns are not immobilizing. As one sponsor noted, there is also a risk in not doing enough to help participants.

We believe that plan sponsors therefore should give serious consideration to adding projections to statements, particularly involving projected monthly income in retirement. These projections should clearly disclose the assumptions upon which they are based. Sponsors with more-sophisticated participants might want to add online projection tools that let participants provide more complete financial data, such as assets outside of their company 401(k), and to vary the underlying assumptions used to generate the projection. Sponsors should also consider adding charts to show the projected difference that an increase in deferral rates would make to monthly income in retirement.

"I think this is a dangerous idea. While I think giving people access to information about how they can stretch their money is good, it's a challenge because the assumptions in these projections are really a best guess."

Plan Sponsor

SIMPLIFIED INVESTMENT MENU

Many plan participants make poor choices when choosing from the typical DC investment menu. According to a recent industry survey, almost three-quarters (74%) of 401(k) participants think it is a good strategy to buy a bit of every investment offered and only two in 10 (18%) think that investing in a target date fund is an ideal way to diversify.[8] We believe that providing fewer, better-diversified choices would promote better asset allocation for all plan participants. Therefore, plan sponsors should strongly consider streamlining the investment menu in a DC plan to a simplified series of objective-based funds essential to investing for retirement, plus a series of target date funds.

FIGURE 7: PARTICIPANT REACTION TO SIMPLIFYING NUMBER OF INVESTMENT OPTIONS

Other employers are interested in simplifying the number of investment options they offer as part of the 401(k) plan. Suppose your employer reduced the total number of investment options in the plan to five plus a series of target date funds. The five investment options would be well-diversified and would include the same asset classes (or potentially more than) your employer currently offers. How would you view this change?

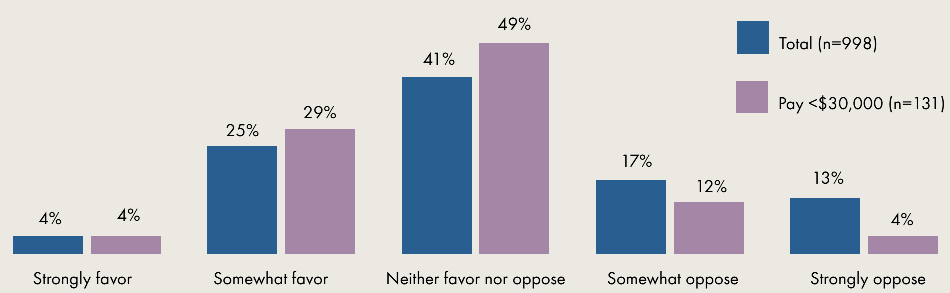


TABLE 1: FRAMEWORK FOR SIMPLIFYING NUMBER OF INVESTMENT OPTIONS

The following table offers one example of a simplified core menu of objective-based funds.

FUND NAME	DESCRIPTION	WHY THIS MAKES SENSE
Growth	A globally diversified strategy that invests in public and private equities, across various market capitalizations, with the goal of exceeding traditional equity returns while maintaining a similar level of risk. This strategy utilizes a core-satellite approach, investing in passively managed public equities while capturing the illiquidity premium through actively managed private equities.	Equities are one of the most essential asset classes for long-term growth. Participants often do not understand how to select or combine equity funds to achieve the fundamental risk-return trade-off necessary, which a strategy with this portfolio objective strives to attain.
Income	A broadly diversified factor-based strategy aimed at generating income through a combination of fixed income and high-quality, high-dividend-yielding equity securities.	Income-producing securities such as bonds or dividend-paying stocks are a crucial component during both the asset-accumulation and retirement (or de-cumulation) phases. Often, participants do not comprehend strategies with an objective to produce income versus more traditional fixed-income instruments. A portfolio of this type, which may be a blend of fixed income and equity securities with a common income goal, can offer a more effective implementation to meet the income objective.
Inflation	A strategy constructed with broadly diversified asset classes demonstrating sensitivity to inflation including U.S. Treasury Inflation-Protected Securities (TIPS), global real estate and commodities.	The impact of inflation on retirement savings is one of the most overlooked elements of portfolio risk by participants. TIPS alone are not an effective strategy to mitigate this risk. A portfolio that combines TIPS with other real assets that have the potential to outpace the impact of inflation may be a more effective defense.
Capital Preservation	A strategy constructed with short-term, highly rated government or corporate fixed-income securities with the goal of preserving principal on a nominal basis while providing steady, positive returns.	Assets in this category are often viewed as the “no-risk” group of investments. Transforming this class from “no-risk” to “low-risk” permits participants to invest in the most conservative option in a plan’s fund lineup. It also lowers portfolio volatility and the risk of large losses and still offers greater return potential than traditional money market instruments.

The Path Forward plan participant survey suggests that most plan participants are likely to accept such a change in an investment menu. (Figure 7.) Only three in 10 (30%) would oppose such a simplification.

Of the five recommendations presented here to improve the DC retirement system, the simplified core menu (as Table 1 shows) is the one that most sharply divides the interviewed plan sponsors, despite strong support from plan consultants. However, they all agree there can be too many investment options and that this can lead to sub-optimal investment performance over time due to confusion, inertia or participants investing evenly across all available options.

Plan sponsors interviewed who support the recommendation think this approach is simpler for participants to understand and is likely to provide better results for unsophisticated investors. "Our menu redesign focused on the 'less-is-more' principle," said one plan sponsor. "As we streamlined from 16 investment options to 7, we focused on simplification and diversification. Participants are no longer overwhelmed by choice – and the construction of our new multi-manager funds provides greater diversification at the option level. We believe that this approach will lead to better asset allocation decisions, and ultimately, to better outcomes in retirement."

Plan sponsors' objections to this type of investment menu tended to center around two factors: (1) the replacement of investment choices based on asset class with objective-based funds and (2) the difficulty of getting buy-in from sophisticated investors.

Most plan sponsors interviewed think it is desirable to reduce the size of their investment menu, but a few feel that they have already reduced it as much as possible. They feel that further reductions would not give plan participants sufficient choice to meet their investment goals. Some also worry about pushback from employees, particularly in companies where the investment menu has been in place for a long time or in highly educated workforces used to navigating a larger number of choices.

Rather than having an objective-based investment menu, many of those interviewed prefer to offer options within each major asset class. These plan sponsors would prefer to use existing, seemingly more-familiar categories such as fixed income or emerging markets and provide participants with one or two choices within each of these classes.

We believe this view is short sighted, given participants' continual struggle to understand asset class-, or "style-box-" based menu construction.

In its 2014 update on 401(k) plans and participants' asset allocations, EBRI noted a wide variability of allocation to equities. According to EBRI, participants averaged a 66% percent exposure to equities. Nearly 44% of participants allocated more than 80% of their balances to equities, while 10% held no equities at all at the end of 2013.

The difficulty getting buy-in for a simplified objective-based investment menu can be addressed in one of two ways. The first is to offer an active and a passive option under each objective-based umbrella. The second is to offer a self-directed brokerage window but include barriers that make it more difficult to select in order to discourage employees who might not have the knowledge to successfully use this option. These barriers could be expressed as some combination of minimum investment amounts required for the self-directed brokerage window, minimum account balances before a window can be opened, limitations on the percentage of the account balance that can be invested, and maximum dollar amounts that can be invested.

Finally, note that plan consultants and plan sponsors do not disagree about whether to reduce the size of the investment menu but rather about how to implement this reduction. Regardless of the actual implementation method, plan sponsors should take a fresh look at their investment menu and opt for fewer, easier-to-communicate options that work for the majority of their plan participants.

"I think it's (simplified menu) a great idea. It's easier for folks that don't have an investment background. It's easier for them to understand and to pick a fund which they think would be best suited for what they are trying to do."

Plan Sponsor

"Our preference is to just go ahead and leave the building blocks out there, and they can go ahead and develop it on their own."

Plan Sponsor

INVESTMENT OPTIONS SPECIFICALLY DESIGNED FOR RETIREES

Many plan participants move their money out of the DC plan when they retire. According to Cerulli Associates, former employees rolled over $321 billion from DC plans to individual retirement accounts in 2012.[9] This often means they manage the money on their own, without any professional financial advice. Only one-quarter (25%) of retirees indicate they received investment advice from a professional financial advisor in 2013.[10] To improve the transition to retirement, plan sponsors should strongly consider adding investment options designed specifically for retirees that would provide professional review of investments at a lower cost than obtainable outside of the plan.

The Path Forward plan participant survey results suggest that many pre-retirees would be interested in such an option. (Figures 8 and 9.) Specifically, 38% would be interested in an in-plan investment option that would provide monthly income guaranteed for life; another 46% would be somewhat interested. Nearly as many (36%) would be interested in an in-plan investment option designed for those who want to begin taking money out of the plan when they retire, with another 47% somewhat interested.

Despite the appetite for retirement investment options among pre-retired plan participants, the responses from plan consultants and plan sponsors interviewed in this research are somewhat more tempered. Most plan sponsors are open to the idea, and many feel their current investment options are not sufficient for de-cumulation needs. They also recognize the pitfalls facing many retirees as they lose access to the advice provided within the plan. While many of these plan sponsors are reluctant to be early-adopters, they are at an exploratory stage regarding whether to add specialized products for retirees.

> *"We know that some of our retirees make unwise choices. Providing strategies for retired plan participants would make DC plans more effective. A need for retirees to get their investments right will definitely grow in the future."*
>
> *Plan Sponsor*

FIGURE 8: PRE-RETIREE INTEREST IN ANNUITY OPTION AT RETIREMENT

Another investment option is designed to provide monthly income guaranteed to be paid out for life. The investment would have an appropriate asset mix specifically designed to produce guaranteed income for life. You would identify when you plan to start taking income and the investment would be designed accordingly. The amount of monthly income received from the investment would be based on the investment balance at the time you begin receiving income. How interested would you be in an investment product such as this?

Over age 55 (n=225)

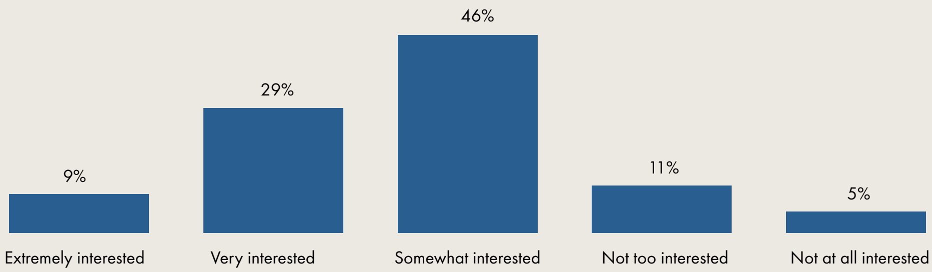
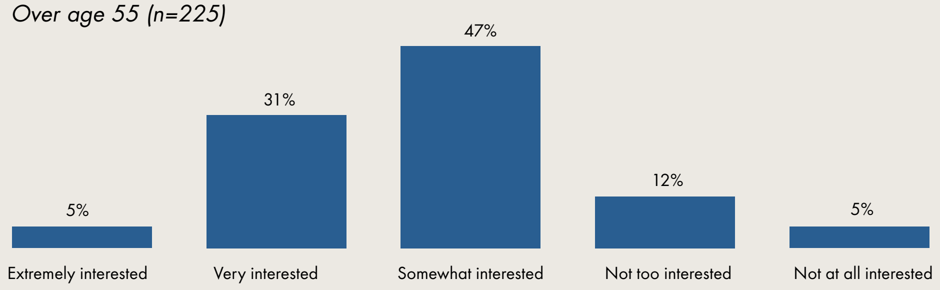


FIGURE 9: PRE-RETIREE INTEREST IN INVESTMENT OPTION FOR WITHDRAWING MONEY IN RETIREMENT

Some employers would like to offer their employees who are participating in the 401(k) plan the opportunity to keep their money in the plan after they retire. To help these employees, the company could offer investment options especially designed for retired people. One example is an investment option specially designed for those who want to start taking money out of the retirement plan, either to help pay their living expenses after they retire or because they are required to start withdrawals at age 70½.

Suppose your 401(k) plan offered an investment option specially designed for people who are retiring. You would identify when you want to start taking out money and, based on that information, the investment would be comprised of an appropriate asset mix designed for retirees with those withdrawal plans. How interested would you be in an investment product such as this?

Over age 55 (n=225)



Plan sponsors interested in investment options for retirees most often mention the importance of addressing longevity risk and providing a stream of predictable/guaranteed income for retired plan participants. They express interest in three options:

- **Income-Generating Funds –** A series of retirement funds designed to support a lifestyle through a focus on income-generation and monthly payments made for a specified period.
- **Guaranteed Lifetime Income –** An account that includes an annuity with guaranteed lifetime income. There would be a charge for the annuity including the cost of the guaranteed income, plus a charge if the account were surrendered within seven years.
- **Personalized Asset Allocation Account –** A flexible personalized asset allocation (i.e., managed account) designed to be appropriate as a person ages throughout retirement.

"I would design an option for retirees that was income-oriented. I think especially in today's low-rate environment, the idea of getting yield or income out of your 401(k) is an area that would require more attention. I prefer a multi-asset class strategy for diversification."

Plan Sponsor

However, plan sponsors must be willing to retain the assets of retired plan participants in order to implement these retirement solutions. Some plan sponsors participating in the research are ambivalent about the desirability of retaining these assets, and this obstacle can be difficult to change if the corporate culture/philosophy is not particularly paternalistic. Interest is also lower among plan sponsors interviewed who also offer a defined benefit plan. But this position can be expected to soften as the number of companies providing new employees with defined benefits continues to decline. Other objections focus on cost and product complexity for retirees, but most feel these are surmountable issues. The optimal investment options for retirees may take a few years to develop, but plan sponsors appear open to including them in their DC plans, and it is clear that they are needed. As more retirees depend on their DC accounts for more of their retirement income, it will become increasingly important for plan sponsors to offer professionally reviewed alternatives for their retirement years.

CONSIDERING TARGET DATE FUNDS WHEN IMPLEMENTING IN-RETIREMENT SOLUTIONS

When deciding to offer an in-retirement option to participants, plan sponsors must also consider the importance of a managed-through versus managed-to target date fund glidepath. A glidepath that continues to de-risk past an assumed retirement age of 65 is an important component in supporting more-effective allocation of retiree DC plan account balances. The mitigation of risk does not stop at age 65 but continues to evolve throughout retirement. Human capital can and should be considered in determining the risk profiles of individual participants and, in aggregate, target date fund glidepath risk.

ABOUT THE RESEARCH

The fifth edition of *The Path Forward* was designed to gain insights into ways to help motivate DC plan participants to save more and plan better for retirement. A second key goal was to understand the obstacles to implementing these ideas and to explore methods of overcoming them.

The research consisted of four phases, each conducted by Greenwald & Associates. The first involved 45-minute in-depth interviews with 10 leading plan consultants on ideas for improving saving and planning behavior and the transition to retirement within the context of the DC retirement system. Also examined were solutions identified in past *The Path Forward* research and by Greenwald & Associates.

Phase two tested key solutions with 25 senior executives at major firms sponsoring DC plans and used in-depth interviews lasting approximately 45 minutes. The goals for this phase were to test reaction and receptivity to the ideas generated in the first phase of the research as well as obtain information about any perceived obstacles. All interviews for the first and second phases of the research were conducted between May 5 and August 8, 2014.

The research then moved to a participant survey for phase three to assess employer strategies for improving retirement preparedness among private-sector workers with a 401(k) plan. Information was gathered between October 2 and October 12, 2014, using a 17-minute online survey. Respondents were recruited from Research Now's online panel. A total of 1,007 individuals participated in the study. To qualify for participation in the study, respondents had to be ages 25-70, work in the private sector and have a 401(k) plan through their current employer. The final data set was weighted by age, education and gender to reflect the distribution of those characteristics among 401(k) plan participants ages 25-70 working in the private sector (based on the 2013 Current Population Survey).

Finally, phase four returned to plan sponsors to obtain reaction to key strategies identified in the previous stages of the research that we believe hold the greatest promise for improving the performance of DC retirement plans. This phase included an additional 18 in-depth interviews averaging 50 minutes in length. These were conducted between December 16, 2014, and February 24, 2015.

Plan Sponsors interviewed as part of the fifth edition of The Path Forward represent DC plans with assets totaling in excess of $350 billion. Northern Trust wishes to thank the plan sponsors and consultants who generously shared their time and insights for this research project.

TACKLING CHALLENGES DC PLANS FACE

In this fifth edition of *The Path Forward*, Northern Trust's seminal research series on the DC retirement system, we focus on three inter-related problems:

(1) chronic under-saving by many participants;

(2) inadequate formal planning and goal-setting; and

(3) ineffective transition to retirement.

In particular, the third point describes participants who often lack a reliable calculation of whether they can actually afford to retire. These participants also use poor approaches to sequence of return risk and devote little thought to how portfolios should change through retirement.

Unadvised workers, who generally have no access to professional, unbiased financial advice outside of the employer and plan provider, find the transition to retirement especially challenging.

To address these systemic problems, Northern Trust identified five strategies that show promise. These were gleaned from in-depth interviews with 10 DC plan consultants and 43 senior executives at large organizations sponsoring DC plans with assets totaling more than $350 billion. We also conducted a survey of 1,007 DC plan participants. The resulting five strategies include:

1. Increasing the employer role in encouraging retirement savings
2. Improving automated plan design features
3. Adding projections to account statements
4. Simplifying the investment menu
5. Adding investment options specifically designed for retirees

Plan sponsors should strongly consider whether they can incorporate these strategies to help their employees achieve a financially secure retirement. While these ideas hold promise, they also encounter resistance due to real and perceived implementation challenges. This edition of *The Path Forward* addressed these concerns and provided real-world actions that plan sponsors can take today.

NORTHERN TRUST DC SOLUTIONS

Our DC Solutions group develops innovative answers to challenges faced by many of the world's largest DC plan sponsors. The clients we work with value our consultative approach to addressing their plan and participant needs. That's why they have entrusted us to manage more than $110 billion and to provide custody and administrative services for more than $275 billion in DC assets, as of December 31, 2014 .

TAKE THE PATH FORWARD

You can learn more about our findings, summarized here, by subscribing to receive updates to our *Path Forward* research.

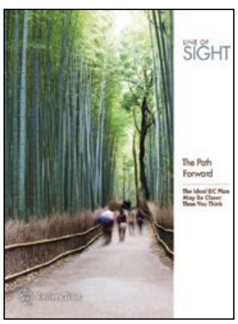
You'll receive insights and recommendations before we release them to the general public. Subscribe today at ***northerntrust.com/pathforward***.

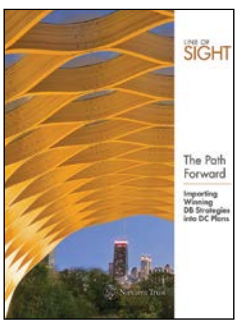
The Path Forward: DC Research Series

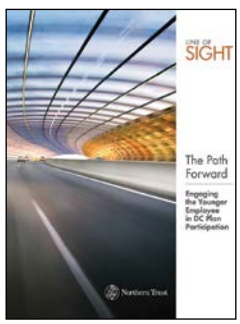
The Path Forward, our annual DC research series, explores topics at the forefront of DC plan design and offers actionable solutions plan sponsors can take – today and in the future – to help their participants achieve better retirement outcomes.

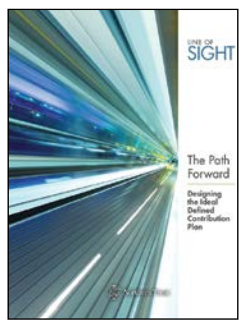
- **Fourth Edition: The Ideal DC Plan May Be Closer Than You Think** uncovers how participants view their DC plan and outlines ways to take DC plans to the next level.
- **Third Edition: Importing Winning DB Strategies into DC Plans** identifies areas where DC plan sponsors can improve their plans by importing DB plan practices and presents "winning" strategies industry leaders are embracing.
- **Second Edition: Engaging the Younger Employee in DC Plan Participation** highlights tactics to address the challenges of engaging employees younger than 35 in DC plan participation.
- **First Edition: Designing the Ideal DC Plan** reveals how DC plan sponsors and investment consultants would design the "ideal" plan and identifies action steps that could be implemented.

Explore our past research and DC capabilities at ***northerntrust.com/dcsolutions***.









ABOUT GREENWALD & ASSOCIATES

Founded in 1985, Greenwald & Associates is a Washington, D.C.-based full-service market research firm with unique industry expertise in financial services, employee benefits and healthcare. They are a co-sponsor of the Employee Benefit Research Institutes's annual Retirement Confidence Survey, now in its 25th year of publication.

ENDNOTES

1 ICI, "Quarterly Retirement Market Data," Fourth Quarter 2014, p. 1.

2 American Benefits Council, 401(k) fast facts, updated April 2014, p. 1.

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4 Helman, Ruth, Nevin Adams, Craig Copeland, and Jack VanDerhei, EBRI Issue Brief, March 2014, No. 397, "The 2014 Retirement Confidence Survey: Confidence Rebounds – for Those with Retirement Plans," Figure 17.

5 Sammer, Joanne, "Sweet Spot: Encourage Deferring Adequate Pay to 401(k)s," SHRM, p. 4.

6 Steyer, Robert, Pensions&Investments, "PSCA: Auto Enrollment and Default Deferral Rates Up in 2013," December 2, 2014.

7 Goda, Gopi Shah, Colleen Flaherty Manchester, and Aaron Sojourner, "Do Income Projections Affect Retirement Saving?", Center for Retirement Research at Boston College, April 2013, Number 13-4, p. 2.

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9 Hechinger, John, BloombergBusiness, "Retirees Suffer as 401(k) Rollover Boom Enriches Brokers," June 17, 2014.

10 Helman, Ruth, Nevin Adams, Craig Copeland, and Jack VanDerhei, EBRI Issue Brief, March 2014, No. 397, "The 2014 Retirement Confidence Survey: Confidence Rebounds – for Those with Retirement Plans," p. 24.

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