Inspired by Innovation

The Actions Early Adopters Are Taking in Their DC Plans

February 2015
Executive Summary

“If you want something new, you have to stop doing something old.”—Peter Drucker

Defined contribution plans have become deeply entrenched as the primary retirement vehicle for most American workers.¹ However, some of the statistics about our savings can be sobering. The Employee Benefit Research Institute (EBRI) recently determined that six out of 10 workers report they and/or their spouse have less than $25,000 in total savings—including 36% who have less than $1,000.² Financial wellness firm HelloWallet determined that 60% of all workers accumulate debt at a rate faster than they’re growing their savings.³

In response, some plan sponsors are taking the reins and heeding Peter Drucker’s advice above. They’re trying something new because they don’t want the old outcomes.

But who are these employers, and what specifically are they doing?

As part of our annual Hot Topics in Retirement survey,⁴ we asked employers to identify where their beliefs on innovation and early adoption fell across a spectrum of possible answers. The group who considered themselves more innovative formed the basis for this paper. Among this group, we found the following:

- Innovators are more likely than the rest of the respondents to have tools in place to assist their employees with improving their financial wellness. They were also far more likely to integrate financial wellness into their physical well-being initiatives (39% versus 20%) and to communicate about the link between financial stress and physical well-being (38% versus 25%).
- Innovators are also taking more actions that are designed to drive as much money in the plan as possible. This could be through boosting participation in the DC plan (encouraging participants to save more).
- Innovators also want to keep as much money as possible in the plan. This is primarily done by discouraging participants from taking loans against their account and having former employees keep their money in the plan. All told, more than one out of three innovators (34%) prefer to have terminated vested employees keep the money in the plan compared to only one out of five (20%) of the rest of the respondents.
- Innovators are more likely to provide their participants with the best tools and funds available for investments. This could be in the form of providing more institutional funds instead of mutual funds (40% of the innovators have institutional funds versus 27% of the rest of the population) or offering more creative fund offerings. Nearly one-quarter of the innovator group (23%) have moved to a custom target-date fund compared to 15% of the rest of the population.

This paper goes into more detail about the innovators’ answers, offering a glimpse into what will increasingly become the norm in the next few years, and suggests some actionable items all plan sponsors may consider to help improve their plans.

¹ Aon Hewitt’s 2015 Trends & Experience in Defined Contribution Plans
² EBRI’s The 2014 Retirement Confidence Survey
³ HelloWallet Debt Savers in Retirement Plans
⁴ Aon Hewitt’s 2015 Hot Topics in Retirement
Identifying the Innovators

There were close to 250 respondents to Aon Hewitt’s Hot Topics in Retirement survey representing a broad cross-section of midsized and larger U.S. employers. One of the questions in the survey was “What statement best describes your organization's attitude toward change within your retirement programs?” with the following options provided:

A. We want to be innovative and be the first to try something new.
B. We don’t like to be the first to adopt a new feature or approach, but are generally among the early adopters.
C. We are not averse to change and will make changes when there is a good track record of success.
D. We make changes only when features are offered by the majority of plans or our competitors.
E. We like consistency and prefer to rarely change the plan.

Together, answers A and B accounted for 23% of the respondents. These 58 organizations became what we label in this report as the “innovators.” For simplicity’s sake, we refer to those who answered C, D, or E as “the rest of respondents” in this paper.

Some statistics on the innovators group:

- In total, these 58 organizations employ nearly 1.9 million employees, but not all were large employers. The range in employee size went from just over 500 employees to well into the hundreds of thousands of workers with a median of 10,000 employees.
- The innovators were not clustered in one geographic region. They were headquartered across the U.S. from Oregon to Florida and from Rhode Island to California.
- There was a broad cross-section of industries represented.
Fostering Financial Wellness

One of the main overall findings from the 2015 Hot Topics in Retirement survey was that 93% of all employers are very likely or moderately likely to create or expand their focus on financial wellness in a manner that extends beyond retirement decisions. Among the group of innovators, the number was 100%, with 57% citing they were very likely to do so in 2015 and another 43% responding they were moderately likely.

The other interesting fact is that many of the innovators are already offering tools, services, and education to help their workers develop more sound financial practices. Across the board, the innovators were more likely to offer different tools and services than the other respondents. Moreover, among the respondents who have not already adopted features, the innovators group was far more likely than the rest of the population to introduce them in 2015.

Prevalence of Financial Wellness Services

Very Likely to Add Financial Wellness Services
The reason for adding financial wellness services at these organizations is sound. When asked whether the importance of financial wellness has increased over the past 24 months, 60% of the innovators stated yes, compared to only 45% of the remaining population.

**Ways to Promote Financial Wellness**

Plan sponsors looking to improve the financial wellness of their workforce can take a page from their efforts on health and wellness initiatives. It’s likely to be a continual process and one that, at times, may feel like a never-ending trek to a destination that’s unattainable. Nonetheless, just as there are certain steps and processes to improve the physical well-being of individuals, there are some best practices for financial wellness initiatives:

1. **Define what financial wellness means to your organization.** There does not appear to be a universally accepted definition of the words “financial wellness.” Work within your organization and with outside experts to construct a definition that works for you and your objectives.

2. **Offer a suite of financial wellness tools, products, and initiatives.** Honing in on one aspect of financial wellness is like saying that the only way to improve health and wellness is by offering a smoking cessation program. While it can help with some, it’s unlikely to apply to the majority of your workforce.

   Offer many different tools, services, and education campaigns that will appeal to a broad variety of workers. Some may need assistance with basic budgeting, while others could use a hand with planning for a home purchase. Some may be trying to figure out how to invest for the first time, and others may be looking at estate planning. Create services that appeal across the diverse needs of your workforce.

3. **Evaluate and revise your financial wellness strategy.** Determine how you want to measure the success of your program(s). Some companies may measure success quantitatively, be it through statistics in the retirement plan (e.g., participation, savings rates, loan usage) or through other measures like employee engagement or reduced absenteeism. Companies could also gauge success by measuring the number of employees who sign up for the service. Any way you cut it, there are likely to be returns on the investment. According to a study from the Consumer Financial Protection Bureau, employers can see a return on investment be anywhere from $1 to $3 or more per dollar invested.5

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5 Consumer Financial Protection Bureau, *Financial wellness at work—A review of promising practices and policies*
Maximizing Retirement Income Security

The innovators are steadfast in their desire to increase the amount of assets invested in the plan, particularly by having many workers participate in the plan and contribute at meaningful savings rates. Nearly three-quarters of the group (74%) said that it was very important to encourage participants to contribute more to help meet their retirement needs. This was more than 20 percentage points higher than the rest of the survey respondents (53%).

Importance of Participant Behavior and Plans to Address in 2015

In addition to focusing on increasing participation, the innovators were also far more likely to report that it was very important to discourage cash-outs and encourage lifetime income.

Defaulting on loans erodes retirement savings. The innovators are searching for ways to educate their participants on how seemingly small loan amounts can have a much bigger impact on retirement income. One-third (32%) are very likely to address leakage in 2015. This is about double the percentage reported by the rest of the respondents (17%). Additionally, the innovators were far more likely to have already taken steps to reduce leakage:

- More than one out of five (21%) innovators recently reduced the number of loans a participant can have outstanding at one time. This is more than four times the percentage of the rest of the survey respondents (5%).
- Another 9% of innovators have recently increased loan origination fees, while only 2% of the remaining group have done so.
- Recently, 61% of innovators allowed terminated participants to continue loan payments, while only 32% of non-innovators allow this.

Reducing Leakage

In addition to focusing on increasing participation, the innovators were also far more likely to report that it was very important to discourage cash-outs and encourage lifetime income.
- Around four out of 10 (39%) are very or moderately likely to require participants requesting a loan to speak with a financial counselor compared to 15% of the others.
- Nearly half (45%) of innovators are very likely to study demographic data on the participants taking loans. This percentage is more than three times the rest of the respondents (12%).

**Promoting Income Solutions**

While it’s very important to have participants accumulate sufficient assets in the DC plan, many plan sponsors also feel it’s important for participants to be able to translate the nest egg into lifetime income. In the *Hot Topics in Retirement* survey, 32% of the innovators rated encouraging lifetime income as very important, while only 11% of the rest of the respondents did.

In terms of products, the innovators are far more likely to offer lifetime income solutions, both in-plan and out-of-plan.

**Prevalence of Retirement Income Solutions**

![Graph showing prevalence of retirement income solutions](image-url)
Ways to Increase the Amount of Assets in the Plan

Plan sponsors looking to increase the amount of assets in the plan can take some of the following measures:

1. **Harness automation.** According to Aon Hewitt’s recent Pulse Survey on Automatic Features,\(^6\) automatic features are gaining in both prevalence and sophistication, but there’s still room for improvement. Twenty-nine percent of plans automatically enroll individuals into the plan at a level high enough to receive the full match, and another 27% have automatic enrollment below the match threshold but have embedded contribution escalation to a level at or above the match threshold. While those are positive signs, it means that close to half of plans do not have mechanisms in place to bring new hires to a rate high enough to receive the full match.

2. **Find innovative ways to communicate to participants about the importance of saving and investing.** Seek out different ways to stress how important retirement savings can be. Target communications to nonparticipants and low savers. Try a multitude of mediums—both high-tech and high-touch—from in-person sessions to text messages to social media. The innovators were more likely than the rest of the respondents to promote participating and saving through text messages (42% versus 34%) and to use games or gamification to promote awareness and understanding of saving and investing concepts (48% versus 34%).

3. **Curb the leakage.** Whether it’s implementing a waiting period between a loan payoff and a new loan origination or reducing the number of loans available to participants, there are structural changes plan sponsors can make to reduce the amount of money that’s flowing out of the plan for nonretirement purposes.

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Improving Savings Options

The innovators are more likely than the rest of the population to help improve their participants’ rates of return within the plan. This is primarily done through two sides of the same coin: reducing fees and streamlining access to professional investing assistance.

Reducing Fund Fees

Whether it’s offering more institutional pricing or taking advantage of economies of scale by negotiating better pricing, the innovators have taken actions that reduce the costs associated with the plan. Ultimately, this makes a positive impact on participant balances. Nearly half (49%) of the innovators recently negotiated more favorable pricing with vendors and/or fund managers compared to 30% of the rest of the respondents.

Actions Taken to Examine/Reduce Fees in the Plan

<table>
<thead>
<tr>
<th>Action</th>
<th>Innovators Completed Recently</th>
<th>Rest of Respondents Completed Recently</th>
</tr>
</thead>
<tbody>
<tr>
<td>Reviewed total plan cost</td>
<td>57%</td>
<td>44%</td>
</tr>
<tr>
<td>Negotiated more favorable pricing with vendors and/or fund managers</td>
<td>49%</td>
<td>30%</td>
</tr>
<tr>
<td>Changed fund option to reduce cost</td>
<td>44%</td>
<td>31%</td>
</tr>
<tr>
<td>Moved mutual funds to Institutional funds</td>
<td>40%</td>
<td>27%</td>
</tr>
<tr>
<td>Added a tier of index options</td>
<td>32%</td>
<td>19%</td>
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Providing Tools

Most participants in defined contribution plans are not professional investors—but time and time again, research shows that experts outperform amateurs. Innovators are far more likely to offer their participants tools such as online guidance, online advice, and managed accounts.

Prevalence of Savings and Investing Tools

1. **Review the fund lineup often or delegate fiduciary responsibility.** Consistently monitoring, benchmarking, and evaluating fund options provides investment committees with the data needed to determine when to swap out funds that are underperforming. However, not all companies have the time or resources for such dedicated monitoring, and some simply prefer to focus their efforts on other issues. In these instances, companies can look to delegate the responsibilities to an outside party. More than one out of four innovators (26%) have delegated investment management to a third-party fiduciary. For the rest of the respondents, the number was closer to one out of 10 (11%).

2. **Use open-architecture, multi-asset funds.** Participants benefit from multi-asset funds because they can streamline choice while providing access to professionally designed portfolio construction. Multi-asset funds can also be used within the core menu to help strike the right balance between having too many funds in the investment lineup and not having enough funds for proper diversification. These “white label fund” vehicles are composed of multiple underlying investments and can introduce certain types of investments to participants without the risk of having individuals overweight the sector. In 2015, 17% of the innovators group had a fund that was composed of multiple funds or multiple managers compared to 11% of the rest of the respondents.

3. **Facilitate access to independent professional investing assistance.** Target-date funds have practically become a given in defined contribution plans, mainly because they allow individuals to receive professional portfolio management in a relatively cost-effective and easy manner. However, over time, age may not be the primary driver for an individual’s investing habits, and these participants may prefer the more personalized, less generic recommendations from online advice, managed accounts, or online guidance. Among the innovator group, these products are the norm, not the exception.

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7 See, for example, Aon Hewitt and Financial Engines’ report *Help in Defined Contribution Plans: 2006 through 2012*
Conclusion

For all of its successes, the defined contribution plan framework can be enhanced. This paper shows how some employers are leading the charge. The “innovators” are taking actions such as incenting more individuals to participate in the plans, improving the rate of savings, discouraging loans and cash-outs, and paving the way to receive professional investing assistance. Ultimately, this will hopefully translate to more retirement income for their participants. We applaud these plan sponsors for their innovation and tenacity, and expect that they’ll pave the way for more plan sponsors to follow in their footsteps.
Contact Information

Rob Austin, FSA, EA
Director of Retirement Research
+1.704.343.4100
rob.austin@aonhewitt.com

Amy Atchison
Research Consultant
+1.847.295.5000
amy.atchison@aonhewitt.com
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