2011 Trends & Experience in Defined Contribution Plans

Paving the Road to Retirement
About This Survey

The Trends & Experience in Defined Contribution (DC) plans survey has been conducted every two years since 1991. The 2011 survey was responded to by a record number of employers—546 across a variety of plan types, sizes and industries. For purposes of this survey the term Defined Contribution (DC) plans include 401(k), profit sharing, 403(b) custodial account, 401(a), 457(b) governmental plans, etc. The survey was fielded in the first quarter of 2011, to understand employer trends relating to retirement plan offerings, design, and investments.

The surveyed plans have a combined total of more than 12 million employees and $780 billion in assets. Thirty percent of the Fortune 500 is represented. The median/average number of employees is 6,000/23,286, and the median/average plan size is $384 million/$1.64 billion.

Note: Percentages in this report are rounded to the nearest whole number; therefore, totals may not equal exactly 100%. While the focus of the survey instrument and survey samples has changed from year to year, there still are a number of areas where useful comparisons and trends over time can be examined.

Survey Highlights

Defined Contribution (DC) plans continue to play an increasingly important role in the future of retirement. The bulk of plans now report the DC plan as the primary source of future retirement income for the employees it covers—this is up significantly from previous surveys. During the past two years, employers have continued to design their DC plans to encourage robust participant savings and investing behaviors, and increase the likelihood that employees can meet their future retirement needs.

Automation—including automatic enrollment, automatic contribution escalation, and automatic rebalancing—has become standard in many DC plans. At least one of these features is now offered by the majority of employers surveyed. However, while automatic enrollment has aided participation levels, the increase has been slow as few employers extend the feature beyond new hires. Furthermore, there is room for improvement in the default contribution rate as the majority of employers set the level low, often beneath the maximum match threshold.
Many companies are offering investment options and advice tools that simplify investment decisions and help employees make better choices. The prevalence of target-date portfolios and outside investment advisory services—including advice, guidance, and/or managed accounts—has increased significantly in the past two years. Regarding investment fund design, there is a focus on a tiered structure and distinct choices for employees. Target-date portfolios are now a staple in the bulk of plans, with eight in ten plans offering them. Further, brokerage windows also continue to gain momentum in meeting the needs of a small subset of the population without overwhelming the majority.

Retirement income solutions have also garnered significant attention in the marketplace, and employers are focusing more on these services. More employers are adopting both in-plan, and out-of-plan services to assist employees in evaluating and meeting their retirement income needs, while more are contemplating future adoption of these solutions.

Finally, plan expenses are top of mind with many employers, with the majority of plan sponsors (63%) indicating they are concerned about the topic. In recent years, fees have gained significant attention among the media, regulators, and litigators. Many plan sponsors have analyzed their current fee structure along with the appropriate way(s) to communicate these messages to employees.

Additional detail on these and other trends are summarized on the following page.

Available Retirement Programs

DC plans are now the primary retirement savings vehicle for the majority of workers, up substantially from 2009. This trend escalated during the previous two years.

Employers continue to evaluate the success of their plans primarily through adequate performance of investments and the adequate facilitation of retirement income for participants, as well as the cost-effectiveness of the plan. This is consistent with 2009 results; however, the performance of investments was ranked higher than historical levels.

Plan sponsors are still gradually moving away from traditional Defined Benefit (DB) plans. About half of respondents cover (some or all) salaried employees under a traditional DB pension plan, as well as the DC plan. Twenty-two percent report that salaried employees are also covered with a hybrid DB pension plan. Altogether, 57% of plans offer both a DC plan and DB pension plan (down from 64% in 2009). Additionally, of those with DB plans, 44% of these plans remain open to new hires, down slightly from 46% in 2009.
In terms of changes to retirement programs, while some employers had cut-backs in their DB plans and/or retiree medical programs during the past two years, many of these same employers have simultaneously enhanced the DC plan. The main form(s) of enrichment reported was introducing a DC matching contribution (13%) and/or nonmatching contribution (10%).

**DC Plan Design Basics**

Ninety-five percent of employers consider their plans subject to ERISA. Among these, 81% report that their plans comply with ERISA section 404(c).

In addition to offering a DC plan to salaried employees, nearly three-quarters of employers offer the same plan to nonunion hourly employees. Eighty-five percent of employers offer the DC plan to their part-time employees; this is consistent with 2009 results though slightly higher than 2007.

Eligibility requirements to participate in a 401(k) plan and to receive a company match remained largely consistent in the past two years. About seven in ten plans (71%) provide immediate eligibility, similar to 2009 levels. Further, for employer-matching contributions, more than half (52%) provide corresponding immediate eligibility as well.

The maximum employee contribution rate continues to climb, with an average rate of 61% (versus 54% in 2009). The threshold of 50% to 59% is the most prevalent among one-third (32%) of plans.

Catch-up contributions are provided among the vast majority of plans, offered by nine out of ten plans.

**Key Findings**

- 95% of employers consider their plan an ERISA plan; 81% of these report their plans comply with ERISA section 404(c).
- 71% of plans provide immediate eligibility in the plan, and 52% provide immediate eligibility for matching contributions.
- 61% is the average maximum employee contribution rate, up from 54% in 2009.
- 92% of before-tax plans allow catch-up contributions, 94% allow among those that also offer Roth.
Employer Contributions

Nearly all (93%) of responding employers contribute employer money to their plans, down just slightly from 95% in 2009. Eighty-five percent provide matching contributions (fixed, graded, service, or other). A fixed match remains most prevalent among 63% of plans, while 18% use a graded match. Further, 29% of employers provide nonmatching contributions.

In 2011, the most common type of fixed match is still $0.50 per $1.00 up to a 6% of pay, with 14% of employers reporting this formula. In total, 19% of plans match $0.50 per $1.00 up to a specified percentage of pay. The second most common type of fixed match is $1.00 per $1.00 up to 6% of pay, reported by 10% of plans. A quarter of plans with a fixed match formula reported a $1.00-per-$1.00 match up to a specified percentage of pay.

Employer contributions continue to immediately vest across 43% of plans; this is static from 2009. The most prevalent vesting schedule remains 3-year cliff vesting (18% of plans), followed by 5-year graded schedule (16% of plans).

Key Findings

93% of plans provide employer monies to the plan, down slightly.

85% of plan sponsors provide matching contributions (fixed, graded, service, or other), and 29% provide nonmatching contributions.

14% of employers offering a fixed match, use $0.50 for $1.00 up to 6%. This is the most popular formula.

43% of plans vest employer contributions immediately.
**Employer Stock**

Employer stock is an investment option among 36% of plans surveyed. Larger employers (those with more than 5,000 employees) are more likely to offer the option, with 52% of these firms offering versus only 18% below this threshold.

Across plans making the investment option available, 93% allow participants to direct their employee contributions in the employer stock fund. The bulk of these plans do not restrict participants, with only 23% of plans restricting participants’ investment in employer stock (by contribution or balance). This is up slightly from two years ago (20%). Among those restricting, increasingly they are doing so at lower thresholds—decreasing the amount of contributions and/or balances that employees may invest in employer stock. The average maximum percentage in contributions is 23%, while the average maximum balance allowable is 22%.

Fewer employers match exclusively in company stock, and this has continued for many years. Among plans that offer employer stock as an investment option, only 12% require matching contributions to be invested in employer stock, down from 17% in 2009 (and down from 36% in 2005). Further, of plans that do match in employer stock, there are far fewer restrictions associated. In 2011, 90% of plans report that participants may diversify employer-matching contributions at any time, up from 84% in 2009 and 46% in 2005.

**Key Findings**

- **36%** of plan sponsors surveyed provide employer stock (52% of larger plans).
- **23%** of plans offering employer stock restrict participant investment in some way.
- **12%** of plans with employer stock, also provide matching contributions in employer stock. Among these, 90% allow for immediate diversification.
**Automatic Features**

Automation has become standard in many DC plans. The percentage of employers that automatically enroll participants has plateaued at 56% of plans, similar to 2009 levels. Among those not offering, 5.5% plan to add during 2011. Companies that offer both DC and DB plans continue to be more likely to automatically enroll employees (62%), compared to those that are DC only (47%).

Although there has been much discussion around the needs for automatic enrollment to also reach existing nonparticipants, still the vast bulk (82%) only default only new hires. This is nearly unchanged from 2009.

Default investments under automatic enrollment have shifted to qualified default investment alternatives (QDIA) options, with target-date portfolios dominating. Currently, 78% of plans default participants’ funds into a target-date fund, up from 69% in 2009 and 50% in 2007. Balanced or target-risk funds are used with 13% of plans, managed accounts by 3%, and stable value or money market by 6% of employers.

Default contribution rates have also been discussed significantly in the marketplace, focusing on whether these rates are adequate given participant inertia. Two-thirds of plans (66%) continue to use a 1% to 3% default rate. These stats have only marginally improved in the past two years, with 15% of plans defaulting at a rate of 6% or higher (up from 12% of plans).

Automatic contribution escalation is also more popular, with 51% of plans offering the feature (up from 44% in 2009), and another 6% plan to add in 2011. Escalation is also more popular as part of automatic enrollment, with 45% of plans using automatic escalation within automatic enrollment (up from 40% in 2009). Escalation is more prevalent among plans that initially default at lower rates (76% default at 2% or 3% of pay initially).

Automatic rebalancing is offered by 53% of plans, up from 47% in 2009. Another 3% of employers report they plan to adopt it during the coming year.

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**Key Findings**

- **56%** of plans now have automatic enrollment, flat since 2009.
- **78%** of plans default participants that are automatically enrolled into age-appropriate target-date portfolios.
- **66%** of plans default participants that are automatically enrolled at a contribution rate of only 1% to 3% of pay initially.
- **51%** of plans offer contribution escalation, and 53% make automatic rebalancing available.
Investment Monitoring

The process of selecting and monitoring investment options continues to be top of mind with employers. Currently, 83% use an external investment consultant to assist in evaluating and monitoring investment options. Nearly nine out of ten plans (87%) have a written investment policy statement, up from 83% in 2007 and 78% in 2005. A written investment policy statement provides a framework for decision making, and 79% of sponsors report that they include a watch-list policy, while 74% include fee-related topics in their statement.

When it comes to selecting funds, fees and expenses were again rated as the most important factor, with 67% of sponsors indicating it is “very important” up from 59% in 2009. Fund investment process was also noted as very important by 65% of employers. Historical performance fell from the top spot in 2007, and is now third, ranked as very important by 63% of plan sponsors. Name recognition and the availability of fund information in public sources were given lower priorities, and noted as very important by only 8% and 12% of sponsors, respectively.

Key Findings

83% of plans use an external investment consultant.

87% of plans have a written investment policy statement.

67% of plan sponsors rank fees as “very important” in selecting and monitoring investment options.

Investment Structure

Plan sponsors have focused their investment structure on more tiering, simplicity, and a base of target-date portfolios.

Fifty-seven percent of employers report using a tiered investment structure to communicate with participants. Among these plans, the most prevalent tiers include target-date portfolios, asset class funds with a mix of active and passive, and a brokerage window or expanded fund set.

The number of funds offered is flat, excluding premixed portfolios (target-date and target-risk funds). Excluding premixed funds, the average number of funds offered declined from 14 to 13 funds, and the median grew from 12 to 13.

Target-date portfolios are now offered by 81% of plans, up from 71% in 2009. Target-risk funds have lost ground again, now available in 10% of plans, down from 18% in 2009 and 32% in 2007.
Among core funds, the most prevalent asset classes remain Stable Value, Intermediate-Term Bond, Large-Cap Equity, Small-Cap Equity, and International Equity. Specialty bond funds also experienced a dramatic increase, up 17 percentage points since 2007, fueled largely by increasing adoption of TIPS funds (Treasury inflation-protected securities). Usage of REITs (real estate investment trusts) has also grown substantially, doubling in prevalence since 2007. Additionally, the adoption of self-directed brokerage windows continues to grow. In 2011, 29% of plans offer self-directed brokerage window, up from 26% in 2009 and 18% in 2007.

Index funds have grown in prevalence across a variety of asset classes and remain prevalent in large-cap equity and intermediate bond. Additionally, nonmutual funds have grown substantially, especially among larger plans. For plans with more than $1 billion in assets, 62% had most of their investment offerings as institutional vehicles, up from 57% of plans in 2009 and 49% in 2007.

Across all plan assets, two-thirds of assets are invested among four broad categories: stable value (20%), premixed portfolios (13%), large cap equity (22%), and employer stock (13%). With the recent large gains experienced in the financial markets, participants’ asset allocations have shifted, primarily due to passive changes/market valuations, and also partly through active transfers to premixed portfolios.

**Key Findings**

- **81%** offer target-date portfolios, up from 58% in 2007.

- **13** funds, is the average and median number of core funds available to participants.

- **29%** of plans offer access to a self-directed brokerage window, up from 18% in 2007.
Investment Education and Advisory Services

Consistent with the historical surveys, investment education and advisory services are increasingly prevalent and top of mind. Nearly all respondents (98%) use written materials for communicating investment concepts, while only 22% report that they are very effective. The most effective media reported is on-site seminars/workshops/meetings (ranked very effective by 54% of plans), followed by call center counseling (38%) and personalized communication (38%).

More companies are helping their employees make wise investment decisions by offering independent financial advice and education. Three-quarters (74%) of plan sponsors now offer outside investment advisory services to employees, up 50% since 2009 (offered by only 50% of plans). The types of services offered range from online advice (37%) and guidance tools (47%), one-on-one counseling (44%), and managed accounts (29%), with increases seen across all. Another 7% of employers note they will provide these types of services in the next year.

Close to half (47%) of employers now offer participants access to online guidance, up from 28% in 2009. Additionally, 44% of plans provide one-on-one financial counseling. Both online advice and managed accounts also increased in prevalence, now offered by 37% and 29% of plans, respectively, and 8% of sponsors are likely to add each solution in the coming year.

Among employers that do not offer outside investment advisory services to their employees, two-thirds report the main barrier being legal/fiduciary in nature. Cost concerns are reported as the primary barrier among 18% of plans.

Key Findings

98% of respondents use written materials for communicating investment concepts.

74% of employers now offer outside investment advisory services, up from 50%.

37% offer online advice.

29% offer managed accounts.

47% offer online guidance.
Plan Expenses

Employer concern over fees has persisted in the past two years, with 63% noting they are very or somewhat concerned about fees, given the recent scrutiny by regulators and litigators.

However, the percentage of plans that have calculated total plan cost (fund, administrative, and trustee fees) has declined since 2009—with 72% of plans calculating last year versus 84% in 2009. Larger plans, with more than 5,000 employees, were more likely to do so than smaller plans. Among those who have not calculated, half (51%) listed complexity as a hurdle, while 23% simply have not made it a priority or have not attempted. Additionally, three-quarters of employers have made efforts to reduce expenses in the past two years, similar to what was reported in 2009.

Regarding administrative fees, 73% of plans report that participants pay all recordkeeping fees, either directly or indirectly. Just under one-quarter of companies (22%) share the fees with participants, and 5% of employers pay all fees directly. The percentage of employers paying all administrative costs fell from 11% to 5% in 2011.

In terms of how fees are assessed to participants, 94% do so across plan assets—including 66% through revenue sharing (only), 11% through add-ons (accruals) to funds, and 17% that combine these approaches. Additionally, 14% of plans charge a periodic line-item fee to participants (including 2% that also charge fees over assets). Add-ons as well as line-item charges have been increasingly used to help more equitably share costs with participants on a consistent basis, especially among larger employers.

Disclosure of fees has become a priority during the past two years, as employers are increasingly using vehicles to illustrate fees, and many are using multiple methods. About half (51%) of plan sponsors say they disclose administration fees in fund fact sheets and/or prospectus information (up from 28%), and now 43% include it with participant account statements (up from 23%). For investment management fees, 85% of plan sponsors note they disclose fees in fund fact sheets and/or prospectus information, up from 60%.

Key Findings

63% of plans are somewhat or very concerned about fees amid the recent scrutiny.

72% of employers report calculating total plan cost in the past year, down from 84% in 2009.
Retirement Income Solutions, Loans, and Plan Distributions

Retirement income solutions have garnered significant attention in the marketplace, and more employers are focusing on these services. More than a quarter of plans (29%) now provide or promote some form of retirement income solutions, either inside or outside their plan. Facilitation of annuities outside the plan is offered by 18% of plans, while 15% of companies report an in-plan solution today, including managed payout funds (offered by 11% of plans), managed accounts with drawdown feature (8%), and annuity within the plan (8%). Another 6% of employers report that they plan to add at least one of these in-plan solutions during 2011. DC-only plans are more likely to provide in-plan solutions—(19%) than companies with both a DC and a DB plan (13%). Additionally, nearly three-quarters of plans provide online modeling tools to help employees understand what they can spend each year in retirement (another 5% are very likely to add in coming year).

Most plans (93%) have a hardship withdrawal provision, and this is consistent with the previous surveys. Further, 90% of plans allow in-service withdrawals for participants who have attained age 59½.

Nearly all of the surveyed plans (94%) have a loan provision, with 98% of these plans offering general purpose loans and 82% offering home loans. It is most common for plans to offer one or two outstanding loans.

Regarding terminated workers/assets, nearly a quarter of employers report they prefer balances to remain in the plan. Larger plans (with more than $1 billion in plan assets) are more likely to have this penchant, with 39% preferring assets to remain in the plan, versus 17% below that threshold. Sixty-seven percent of all plans report they have “no preference.”

Key Findings

- 29% of respondents provide some sort of income solution—18% offer facilitation outside of the plan, while 15% offer an in-plan solution.
- 94% of plans have a loan provision.
- 90% of plans allow in-service withdrawals.
ADP/ACP Testing

Three out of ten employers (33%) report using a safe harbor design in lieu of ADP/ACP testing, up slightly from 31% in 2009. Among those that use a safe harbor design, 11% use the pre-Pension Protection Act safe harbor formula while 22% use the Pension Protection Act safe harbor formula.

Three in five plan sponsors (61%) expect to pass the 2010 ADP test without adjustment to highly compensated employees’ (HCEs’) contributions. At the same time, one in five plans (21%) anticipate limiting the percentage of pay HCEs may contribute in order to pass the nondiscrimination test.

**Key Findings**

- **33%** of plan sponsors use a safe harbor design instead of ADP/ACP testing;
- **11%** use the pre-PPA safe harbor formula, while **22%** use the PPA formula.
- **61%** of plans undergoing testing expect to pass it.

Participating Employer Information

Over a third of employers have 10,000 or more employees. The median size of participating employers is 6,000 employees, and the average size is 23,286 employees. Twenty five percent of employers that participated in this survey are ranked as Fortune 500 companies. About one-third of plans have more than $1 billion in total plan assets. On average, participating plans have assets of $1.64 billion. The median assets are $384 million.

A variety of industries are represented in the survey, including financial services (8%), health care (8%), and energy/utilities (7%).

**Key Findings**

- **546 plans** were surveyed, representing more than 12 million employees and $780 billion in assets.
- The median size of respondents is 6,000 employees, and the average size is 23,286 employees.
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