

# 2014 Universe Benchmarks

Measuring Employee Savings and Investing  
Behavior in Defined Contribution Plans

## Highlights



## About This Material

Aon Hewitt is pleased to present the *2014 Universe Benchmarks* report. This report analyzes the participant behavior of more than 3.5 million employees eligible for defined contribution plans offered by their employers. The data can be used to provide a comprehensive view of the defined contribution universe including participation rates, savings levels, plan balances, investment actions and account activity.

The findings from this report can be used by plan sponsors in a variety of ways:

- **Benchmarking.** Plan sponsors can compare how their workers' savings and investing behavior compares to that of participants at other organizations.
- **Plan design.** Employers can better understand general patterns of participant behavior across demographic groups to determine who might benefit from certain plan features.
- **Communication.** Demographic analysis helps plan sponsors pinpoint which groups of workers may benefit from correspondence on particular details of the plan.

## Background

This analysis, dating back to 2002, examines the savings and investing behavior of 3.5 million eligible employees across 144 defined contribution plans, with an average of 24,700 eligible employees per plan.

Below is an overview of plans included in *2014 Universe Benchmarks*.

- The vast majority offered some type of employer-matching contribution in 2013
- 58% offered after-tax contributions
- 20 funds offered on average when premixed portfolios were counted individually; 14 on average when premixed portfolios were counted as one option
- 91% offered premixed funds
- 58% offered company stock as an investment option
- 39% offered self-directed brokerage accounts (SDBAs)

The average eligible employee in the resulting analysis:

- 43 years of age
- \$57,830 annual salary
- 9.1 years of tenure
- \$91,060 total plan balance

## Overview of Findings

More than three-quarters of employers rely on defined contribution plans as the primary retirement income plan<sup>1</sup> option for their employees, which places the responsibility of growing retirement income back into the hands of individual participants. In the *2014 Universe Benchmarks* report, we found some participant and plan trends moving overall in a positive direction:

- Participation rates across companies continue to grow and reach higher levels than ever before.
- The average plan balance at year-end 2013 eclipsed the previous record high by a large margin, a feat fueled in no small part by the equity bull run throughout 2012 and 2013.

Despite these positive findings, challenges remain. Most participants in the plan are well behind the savings milestones that would indicate they are “on track” to receive an adequate income after retirement. Additionally, they were not actively engaged with their program—only a few changed their savings rates or rebalanced their portfolios during 2013.

This report is based on data from over 140 large employer plans covering more than 3.5 million eligible employees, and analyzes multiple facets of defined contribution behavior including participation and savings rates, plan balances and rates of return, investment portfolios and account activity. What follows are descriptions of findings, brief analyses and comparison data related to each of these categories.

## Participation and Savings Rates

- **The average participation rate across all companies was 78.3%.** This is a slight uptick from last year’s value of 78.0% and well above the value of 69.8% 10 years ago. This result was clearly aided by the increased use of automatic enrollment:
  - Plans with automatic enrollment saw their average participation rate grow to 84.6%, up from 81.4% the prior year.
  - Conversely, the average participation rate among plans without automatic enrollment decreased from 63.5% to 62.4%.
- **The average savings rate was steady at 7.5%.** While more individuals increased their savings rates than decreased their savings amounts, the amount of the increases was smaller than the magnitude of the cutbacks—resulting in an average savings rate unchanged from the year before.
- Roth contributions continue to gain favor among participants. When the feature is available, **11.0% of participants contribute to a Roth account**, up from 9.6% last year and 8.1% in 2011.

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<sup>1</sup> Aon Hewitt 2013 Trends & Experience in Defined Contribution Plans

## Plan Balances and Rate of Return

- **The average plan balance at year-end 2013 was \$91,060**—an ample increase from last year's \$81,240 and \$74,380 at year-end 2011.
- This increase was spurred on by the market—in **2013, participants earned a robust median rate of return of 17.7%**. Over the past three years, the median annualized return was 9.4% and over the past five years, the median annualized return was 13.3%.
- Expressed as a multiple of pay, the average plan balance is 1.2 times pay, up from 0.9 times pay in 2012. To maintain the same standard of living in retirement, an individual needs retirement resources (in addition to Social Security) valued at 11 times pay, on average, assuming a retirement at age 65.<sup>2</sup>

## Investment Portfolios

- Premixed portfolios, both the target-date and target-risk varieties, are the default investment option for many plans and thus receive the lion's share of new participant investments. As a result, this year's report showed an increase, on a participant-weighted basis, in these accounts—**42.2% of participants' portfolios are invested in premixed funds**, compared to 39.7% the prior year.
- Driven in part by the growth in premixed portfolios and in part by the equity rally over the past several months, **the percentage of equities in participants' portfolios has reached an all-time high of 70.6%**, up from 68.3% last year and 59.0% at its nadir in 2008.
- Participants continue to invest in their companies' stocks through the defined contribution plan. Overall, nearly 40% of plan sponsors offer employer stock as an available investment option.<sup>3</sup> Within plans allowing this investment, **the average employee allocation to company stock was 12.9%**, a modest decrease from 13.8% last year.

## Account Activity

- Even though investment markets have been very active over the past few years, participants in defined contribution plans have been relatively quiet when it comes to trading and rebalancing. In 2013, **16.1% of participants initiated a trade**. This percentage is greater than the 2012 value of 14.5%, but well below the pre-recession levels of nearly 20%.
- Among individuals holding assets in premixed portfolios, only slightly more than half (51.5%) are fully invested in these accounts, which are designed to be a turnkey solution.
- **More than one-quarter (26.1%) of participants have a loan outstanding against their defined contribution account**. The average outstanding balance represents nearly one-fifth (19.6%) of the total account.

<sup>2</sup> Aon Hewitt *The Real Deal: 2012 Retirement Income Adequacy at Large Companies*

<sup>3</sup> Aon Hewitt *2013 Trends & Experience in Defined Contribution Plans*

Armed with these data points, plan sponsors may focus on specific actions to improve their plans' statistics.

## Ideas to Increase Participation and Savings Rates

- 1. Enhance automation.** Automatic enrollment can greatly increase participation rates, but low default contribution rates drag average savings rates down. This is further compounded when automatic enrollment is not paired with automatic contribution escalation. The average savings rate among plans without automatic enrollment is 7.9%, but declines to 6.6% when automatic enrollment is present because too many sponsors set the default rate too low. Setting defaults at robust levels or coupling automatic enrollment with contribution escalation will close the gap between these rates.
- 2. Backsweep nonparticipants.** According to Aon Hewitt's *2013 Trends & Experience in Defined Contribution Plans* report, 19% of companies enrolled eligible nonparticipants when implementing automatic enrollment and only 34% of this fraction did this so-called "backsweep" more than once. Because employees need to participate in the plan to realize retirement savings, employers can reinforce the message that building retirement savings is important—and counter the effects of inertia by bringing all nonsavers into the plan and forcing them to opt out if they do not wish to participate.
- 3. Stretch the match.** Nearly one-third (30.3%) of participants save at a level exactly equal to the maximum employer-matching contribution, showing that employees are taking cues from plan sponsors on how much to save. In light of this, employers can consider requiring participants to save more to receive the same matching dollars. For example, employers offering a dollar-for-dollar match on 3% could consider a 50-cents-per-dollar match on 6% to encourage their employees to save more without increasing company costs to the plan.
- 4. Add Roth provisions.** In 2013, participants who use the Roth 401(k) savings feature saved more on average than their non-Roth-using counterparts: 10.2% vs. 7.7%, respectively. Because every dollar in a Roth account yields more retirement income than a dollar in a before-tax account, individuals will save more if they change from before-tax contributions to Roth contributions while maintaining the same contribution levels.
- 5. Target communications.** Plan sponsors can improve the relevance of communications by targeting their message to the needs of the audience. For instance, plan sponsors may consider sending specific communication to nonparticipants with easy steps on how to enroll, and a different communication to low savers letting them know they are not taking full advantage of the resources available. Most plan sponsors agree that sending behavior-focused targeted messages to individuals is an effective way to drive behavior.<sup>4</sup>

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<sup>4</sup> According to Aon Hewitt's *2013 Trends & Experience in Defined Contribution Plans* report, only 4% of those surveyed rate targeted communications as "not very effective."

## Ideas to Improve Investment Returns or Diminish Risk

- 1. Review the funds.** Participant investment portfolios are only as good as the underlying funds available. Plan sponsors that have not performed a fund review in the last few years should consider examining the lineup, paying particular attention to items such as whether an active or passive strategy is best, whether institutional funds are a better option, and how fees relate to performance. Companies may also consider delegating their investment decisions to a third party to streamline and expedite the fund review and change process.
- 2. Re-enroll participants into premixed portfolios.** After years of being told about the importance of investment diversification, participants may feel they are getting a mixed message when they are urged to go all-in on premixed portfolios. As a result, only about half of individuals who have assets in premixed funds are fully invested in the fund. Because these are designed to be fully diversified portfolios, having additional asset classes may counter the goals of the premixed portfolio. In a nod to the power of stout defaults, plan sponsors that are concerned about individuals misusing the premixed portfolios can re-enroll all participants into the age-appropriate portfolio and require the individual to opt out to another asset allocation if he or she so desires.
- 3. Broaden investment advisory assistance.** Plan sponsors should offer services that pave the way for participant access to professional investment assistance, and these methods should go beyond merely premixed portfolios. Online guidance provides assistance to individuals based on asset classes, personalized advice recommends specific plan investments, and managed accounts allow individuals to turn investment decisions over to a third-party professional. All are helpful tools designed for a different target audience, and each is growing in popularity.
- 4. Limit company stock as an investment option.** Even though there has been a steady decline in the percentage of participants investing in company stock, more than half of all participants have some money allocated to employer stock when that investment option is available. Of these, 46.2% have at least 20% of their balance in company stock. According to Aon Hewitt's *2013 Trends & Experience in Defined Contribution Plans* report, one-third of plans (31%) with employer stock as an investment option place limits on future contributions or how much stock a participant can hold at any one time.
- 5. Evaluate lifetime income solutions.** Retirement income solutions have been slow to catch on in defined contribution plans, but they are the only mechanism that allows individuals to insulate against longevity risk. With fewer individuals receiving retirement checks from pension plans, annuity products in defined contribution plans can quell participants' concerns by providing the predictability and stability of lifetime income.

## Ideas to Decrease Leakage

- 1. Encourage a “cash-in.”** Throughout 2013, 43.2% of participants who terminated employment cashed out their retirement accounts. Plan sponsors should urge individuals to roll their balances into their new employer’s plan when they switch jobs. The new hires will make it easier on themselves by consolidating assets, and the plan sponsor may benefit from having more assets in the plan, which could open doors to more preferred asset classes.
- 2. Disallow loans on employer money.** The vast majority of plans allow individuals to take a loan against the balance, and most allow access to assets whether they were derived from employee deferrals or employer contributions. However, when employers restrict the loans to only the balances formed through employee contributions, the average outstanding loan balance is smaller and the percentage of individuals with an outstanding loan decreases.<sup>5</sup>
- 3. Reduce the number of loans available.** There is no standard structure to plans’ loan provisions, and there is wide disparity in terms of the number of loans a participant can have outstanding at any one time. At year-end 2013, nearly three out of every 10 participants (28.7%) had multiple loans outstanding. By limiting the number of loans available, the potential for leakage decreases.
- 4. Add a loan direct debit repayment option.** Very few (3.6%) actively employed individuals defaulted on their loan in 2013. However, once participants terminated employment, the default rate skyrocketed to 64.9%. Some plan sponsors have decided to curb this behavior by providing participants with the option to make loan repayments from a personal bank account. This so-called “direct debit repayment option” allows individuals to continue making loan payments to the plan administrator when payroll deductions are no longer possible.
- 5. Increase loan origination fees.** According to Aon Hewitt’s 2013 white paper *Minimizing Defined Contribution Plan Loan Leakage*, more than three-quarters of employers charge participants a loan origination fee. The most common charge is \$50, followed by \$75. Among the few plans that charge \$100 or more, the percentage of individuals with an outstanding loan dropped, and the average outstanding balance was nearly 45% less.

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<sup>5</sup> Aon Hewitt white paper *Minimizing Defined Contribution Plan Loan Leakage*, October 2013

**Contact Information** **Rob Austin, FSA, EA**  
Director of Retirement Research  
Aon Hewitt  
+1.704.347.0100  
rob.austin@aonhewitt.com

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