

PLANSPONSOR[®]

Regaining Control

Defined contribution plan sponsors are taking a more institutional, “DB-like” approach to DC plan administration

The decline of defined benefit (DB) plans—particularly among larger employers—has precipitated an increased focus from legislators, plan providers, and plan sponsors to redesign and enhance defined contribution (DC) plans, increasingly giving them features like those in DB plans to help fill the gap in retirement savings.

Not that long ago, plan sponsors were essentially discouraged from active and direct involvement in participants’ 401(k) investment decisions. Plan fiduciaries found themselves walking a fine regulatory line where 401(k) “education” was encouraged, but many found the weight of the associated fiduciary responsibility too heavy. Five years ago, there were a couple of lifecycle fund products in existence, but they had not found their way into many investment lineups, and retirement income products were practically unheard of in workplace plans. Wage garnishment restrictions barred the adoption of automatic enrollment programs in some states until the passage of the Pension Protection Act of 2006.

In a post-Pension Protection Act world, DC plan sponsors have more freedom (and perhaps more pressure) to make a real difference in the retirement saving habits of the U.S. workforce. With DB plans, eligible workers were automatically enrolled without the option of opting out. DB participants had no involvement in plan investments or administration, leaving the duties of asset allocation, rebalancing, risk management, fee comparison, and manager selection to plan sponsors.

DC plans, in their most basic form, transferred all such duties squarely to participants, the vast majority of whom were (and still are) ill-equipped to make complicated investment decisions. “The defined contribution plan, initially constructed as an incremental savings vehicle to be managed by an individual participant, has become the primary retirement vehicle for most working Americans,” explains William Wechsler, Principal at Greenwich Associates. “This evolution has necessitated more paternalism on the part of employers,” he adds. DC plan sponsors

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recognize this and, today, many plans are becoming more “institutional,” or DB-like.

One of the first signs of the “institutionalization” of the DC plan is the fact that automatic enrollment programs are becoming more prevalent (up from 17% in 2006 to 23% this year in the *PLANSPONSOR* Defined Contribution Survey). The use of automatic deferral increases took a big jump this year as well, from 6% of plans in 2006 to 12% this year.

Not only are plan sponsors taking a more active role in getting employees to save, they also are trying to make sure that, once participating, employees are investing their money wisely. Asset allocation and target-date products have exploded onto the DC scene. *PLANSPONSOR*'s Defined Contribution Survey indicates that nearly 60% of DC plans currently offer lifecycle funds, and another 20% plan to offer them in the next 12 months. Lifecycle funds are already the default investment in 40% of all plans and more than 53% of large plans that have automatic enrollment. **“The most important change resulting from the PPA, in my opinion, has been the acceptance of auto-enrollment and target-maturity funds as the defaults in employer-based defined contribution plans,”** notes Olivia S. Mitchell, Executive Director of the Pension Research Council at The Wharton School.

Within the lifecycle funds category, the survey shows that 87% of the products offered in DC plans are age-based, compared to 28% that are risk-based—a fairly dramatic shift from last year’s stats of 46% and 55%, respectively. “The funds that were first to market have been big asset gatherers. As the adoption of age-based products continues to ratchet up, we believe plan sponsors, end-user participants, and the consultant community will demand an increasing amount of refinement to these one-step products,” notes Russ Shipman, Managing Director and Senior Vice President of Janus’ Retirement Alliance Services business.

When it comes to asset allocation funds, the survey results show that investment performance is the most important evaluation factor that goes into the selection of lifestyle funds in the plan (scoring 6.27 out of 7 in terms of importance), while risk profile was ranked

METHODOLOGY

In conjunction with *PLANSPONSOR*, Janus Capital Group developed a series of questions for defined contribution plan sponsors specifically pertaining to DC plan investment evaluation, selection, and monitoring as well as overall plan oversight. These questions were included in the *PLANSPONSOR* 2007 Defined Contribution Survey questionnaire. A selection of the answer results is shown below and on the following pages. For more information, please contact surveys@plansponsor.com.

When consultants are used

Fund fee/expense analysis	23.6%	
Fund monitoring	21.8%	
Plan design	18.7%	
Enrollment meetings	9.9%	
Participant education	10.5%	
Investment policy statement design	19.6%	
Investment policy statement monitoring	19.1%	

How often investment options are reviewed

Quarterly	28.4%	
Twice a year	16.5%	
Annually	39.6%	
Every 1-2 years	6.0%	
Every 2-3 years	2.9%	
Every 3+ years	1.8%	
Never	3.0%	
Other	1.8%	

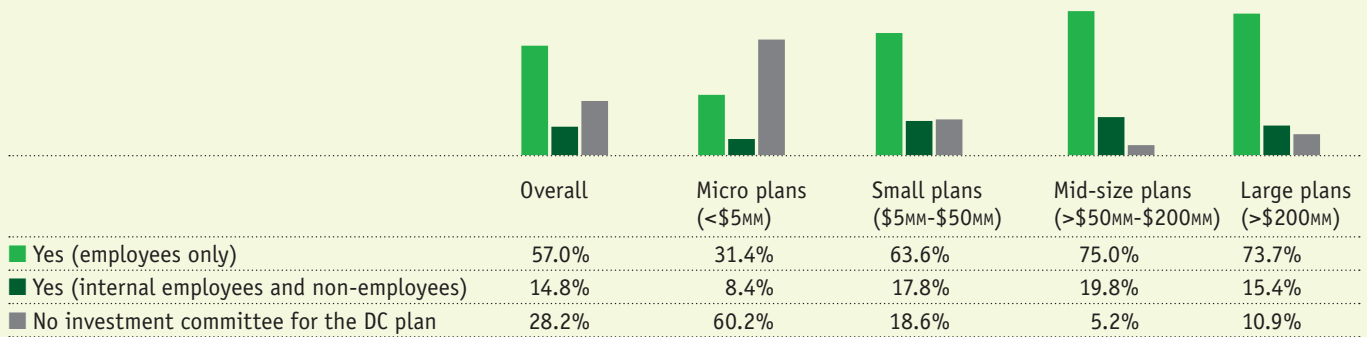
How often plan sponsors meet with investment manager in the plan

Annually	35.2%	
Every 1-2 years	4.4%	
Every 2-3 years	1.6%	
Every 3+ years	1.2%	
Never	45.9%	
Other	11.7%	

How often plan sponsors formally review costs/fees

Annually	69.4%	
Every 1-2 years	11.7%	
Every 2-3 years	6.4%	
Every 3-5 years	5.3%	
Every 5+ years	2.4%	
Never	4.8%	

Investment committee for the DC plan



second most important at 6.00.

What does all of this mean for the future of the DC marketplace? “As plan sponsors continue to assume more responsibility for DC plan administration, we believe there will be an increased demand for superior investment managers, and undoubtedly there will be increased scrutiny on underlying managers in target-date funds,” says Nancy Holden, Vice President of Client Relations for Janus’ institutional business (JanusINTECH Institutional Asset Management). Wechsler adds, “There will be more accepted ways to measure the effectiveness of both the asset allocation of target-date funds as well as the underlying managers within these funds. Open architecture, or the ability to select best-of-breed managers for a target-date fund, is an inevitability as plan sponsors become more educated and benchmarks are standardized.”

However, since many target-date funds are so new, evaluation and comparison of the different funds is currently challenging, at best. Mitchell concurs, acknowledging that, “A challenge will be to develop useful benchmarks. These are evolving, as the funds’ underlying asset mixes and glide

paths mature.” These struggles were described by many in this year’s survey. One respondent notes, “These age-based funds are so new that there is a measure of educated guess about which vendor will produce the most effective product. We will continue to watch ours perform against the evolving benchmarks.” Another survey respondent remarks, “The asset allocation targets at retirement age are all over the lot, making comparison among different providers meaningless.”

Legislative changes also are driving plan sponsors toward lower fees and increased fee disclosure, which will likely spur changing preferences in investment vehicles for many DC plans down the road. “Despite the fact that 66% of plans currently use mutual funds and the survey shows relatively little interest to add other vehicles in the coming year, we share the same view as many industry experts: that the demand for collective trusts and separate accounts will increase in the coming years,” says Shipman. “This year’s Defined Contribution Survey clearly shows that the DC marketplace is becoming more institutional in nature. However, we’re in the early stages of this evolution—and with change come challenges,” adds Holden.

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SURVEY SPOTLIGHT

Investment vehicles used for the DC plan

Separate Account	10.0%	
Managed Account	11.0%	
Commingled Pool	1.6%	
Collective Trust	11.4%	
Mutual Funds	66.1%	

Written investment policy statement (IPS) in place

Overall	72.6%	
Micro plans (<\$5MM)	53.2%	
Small plans (\$5MM-\$50MM)	76.4%	
Mid-size plans (>\$50MM-\$200MM)	88.3%	
Large plans (>\$200MM)	85.0%	

Importance of factors for selecting lifestyle fund(s):

(1-7 scale, 1=not important, 7=extremely important)

Investment Performance	6.27	
Risk Profile	6.00	
Reputation of Fund Family	5.99	
Recommendation of Financial Adviser	5.94	
Experience of Funds' Portfolio Managers	5.89	
Fees	5.79	
Glide Path*	5.77	
Recommendation of DC Provider	5.60	

* *i.e., how the fund adjusts as participant nears retirement*

Types of investment options used currently

Target-Date Lifecycle Funds	36.1%	
Managed Accounts	23.2%	
Risk-Based Lifecycle Funds	22.3%	
Real Estate	14.0%	
Self-Directed Brokerage	15.0%	
Employer Stock	9.1%	
Alternative Investments*	2.0%	
ETFs	0.9%	

* *Hedge Funds, Venture Capital, Private Equity*

Types of investment options planned to be added in next 12 months

Target-Date Lifecycle Funds	15.2%	
Managed Accounts	7.1%	
Risk-Based Lifecycle Funds	5.9%	
Real Estate	3.3%	
Self-Directed Brokerage	3.3%	
Employer Stock	1.6%	
Alternative Investments*	1.1%	
ETFs	0.9%	

* *Hedge Funds, Venture Capital, Private Equity*

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