CALLAN INVESTMENTS INSTITUTE

2010 DEFINED CONTRIBUTION TRENDS SURVEY

GETTING THE DC PLAN BACK ON TRACK

JANUARY 2010

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Executive Summary

What a difference a year can make. In 2009, defined contribution (DC) plan sponsors mainly found themselves performing triage on their plans—stepping up monitoring and evaluation of fund performance in the wake of the market collapse, calming plan participants' fears and determining how to cut plan-related expenses. Going into 2010, plan sponsors are seeking ways to reposition their plans following the market crisis to avoid future pitfalls. Callan Associates' *2010 Defined Contribution Trends Survey: Getting the DC Plan Back on Track* explores trends in DC plan investments, design, communication and delivery. Conducted in late 2009, this survey includes responses from 90 plan sponsors. Sponsors were asked about 2009 DC plan experiences, as well as anticipated changes for 2010. The survey also offers comparisons to Callan's *2007* and *2008 Defined Contribution Trends Surveys*, where relevant.

During the worst of the 2008 market collapse, fund/manager due diligence ranked as DC plan sponsors' number one area of focus. However, going into 2010, strategic initiatives have risen in importance, including plan fees (now tied with fund/manager due diligence as the highest priority), investment structure and plan design. Other key findings of this survey include:

Defaults and Target Date Funds

- Most DC plans now have a qualified default investment alternative (QDIA), and target date funds are the clear QDIA of choice.
- In 2009, 69.3% of plan sponsors report that a target date fund is their default, up from 59.3% in 2008. The increase is notable considering the tough year target date funds experienced in 2008 when their divergent returns drew regulatory and legislative scrutiny.
- Target date funds with a mix of active and passive underlying investments are most prevalent (37.3%), but not by much—35.3% of plans offer active-only target date funds, while 27.5% offer passive-only target date funds.

Core Investment Funds

- Nearly two-thirds (61.5%) of plan sponsors conducted an investment structure evaluation in 2009. In redesigning investment structure, more plan sponsors increased the number of funds (28.1%) than decreased them (14%).
- Real return/TIPS funds were the most common fund additions in 2009, reflecting growing concerns about inflation. Target date funds were the second most common addition, with their popularity undiminished despite market stresses. Domestic fixed income was also a common addition, as plan sponsors sought to provide additional investment diversification opportunities for risk-averse participants.
- Small/mid cap equity was the most commonly eliminated fund in 2009, likely the result of the extraordinarily poor performance of active small/mid cap managers in the third quarter of 2008.
- Real return/TIPS and target date funds were also cited as anticipated additions in 2010 among sponsors considering adding options.

Fund Vehicles

- Mutual funds dominate (93.2%) as an available investment vehicle. However, more than half (52.7%) of plan sponsors also use collective trusts (often the stable value fund) and over one-third use separate accounts (37.8%).
- While there is much talk about exchange-traded funds, only 4.1% of plans offer these vehicles, which are generally not well-suited to large DC plans.

Active Versus Passive Investments

- The vast majority (87.7%) of plan sponsors describe their fund menu as a mix of active and passive funds, with only 4.1% of plans offering a passive-only menu and 8.2% offering an active-only menu.
- At the same time, 17.9% of plan sponsors report increasing the number of passive funds in their plan's menu in 2009, and 17.6% say they will do so in 2010.

Plan Design and Delivery

- Nearly one in five (18.7%) plan sponsors either reduced or eliminated their company matching contribution in the past 12 months. For 2010, about 8% intend to do so. However, 58% of those who reduced or eliminated the match say they will reinstate it within the next 12 months. Nearly 14% are not sure what the fate of the match will be next year, down from one in five who were unsure in 2008.
- Adoption of auto features has plateaued recently. Just under half (43.9%) of plans offered automatic enrollment in 2009—a figure that has not changed much since 2007, indicating little additional appetite under recessionary conditions for this feature. Likewise, the proportion of plans offering automatic contribution escalation has stagnated at about one-third over the past several years.
- Few plans offer retirement income solutions, such as annuities or drawdown services. Adoption of in-plan annuities remains low at 4.3%. Further, only 7% of plan sponsors say they are very likely to add in-plan annuities in 2010. Going forward, online drawdown modeling services, which generally have a low level of fiduciary implications, are the most likely retirement income solution to be added in 2010 at 16%.

Plan Fees

- Virtually all of the plan sponsors in the sample had calculated the fees of their DC plan within the past 24 months (93.3%), with the majority (84%) having done so within the past year.
- Most plan sponsors that calculated plan fees also benchmarked them (81.7%), a material increase from 2008 (76.5%).

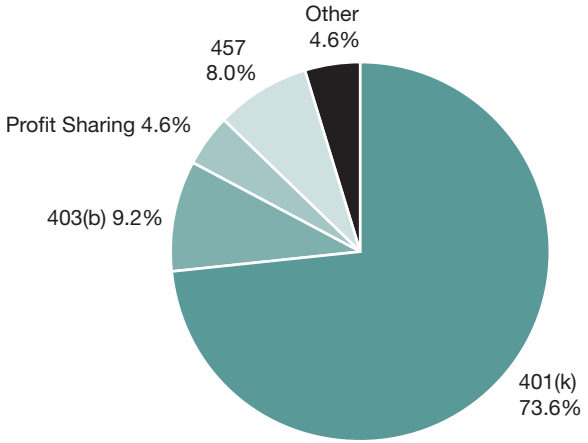
Communication

- Nearly all plan sponsors (or their recordkeepers) engaged in special communication to participants in 2009 (90.7%).
- Over one-third (37.8%) involved communication or education about plan fees. Investing is another area of communication focus cited in both 2008 and 2009.
- For 2010, about two-fifths (39.2%) of respondents will increase the level of participant communication. Investment topics, such as market activity, use of funds, diversification, market timing and target date communication, will continue to be a primary focus (96.6%) followed by retirement income adequacy and contribution levels (63.3% each). Increasing communications around contribution levels relative to 2008 are likely due to concerns about decreased participant deferral rates in light of tough economic times and the fallout from elimination of company contributions (participant deferral rates tend to decline when company matching contributions are eliminated).

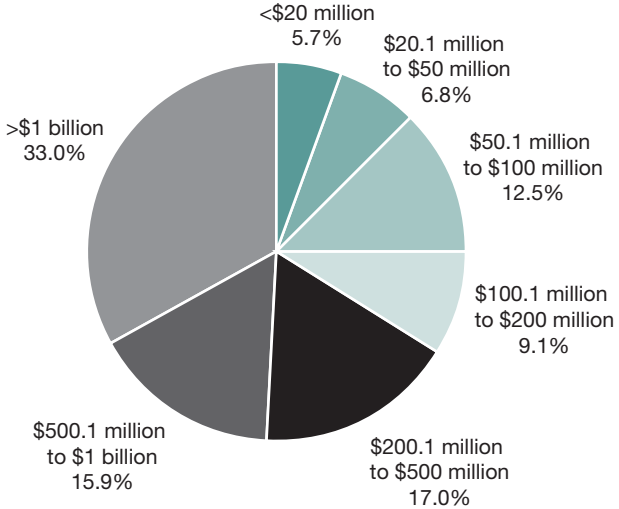
Respondent Characteristics

Callan conducted the online *2010 Defined Contribution Trends Survey* in September and October of 2009. Results incorporate responses from 90 companies, the majority (73.6%) of which offer 401(k) plans. Nearly one in 10 respondents have 403(b) plans—twice as many as in the 2008 survey. The majority of plans have more than $100 million in assets and one-third have assets of more than $1 billion. Just over half (54%) view their defined contribution plan as the primary company retirement plan. Individuals completing the survey typically work in a treasury/finance role, 35% are in human resources and 11% are in legal.

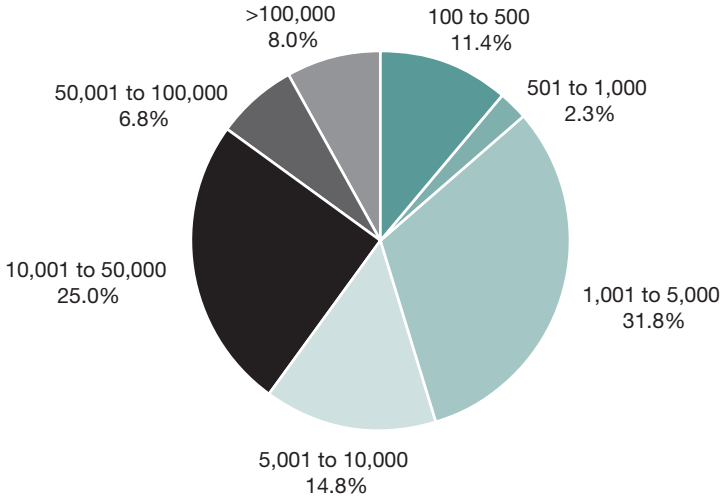
What is the primary DC plan that you offer?



What is the size of your primary DC plan?



How many participants are in your primary DC plan?



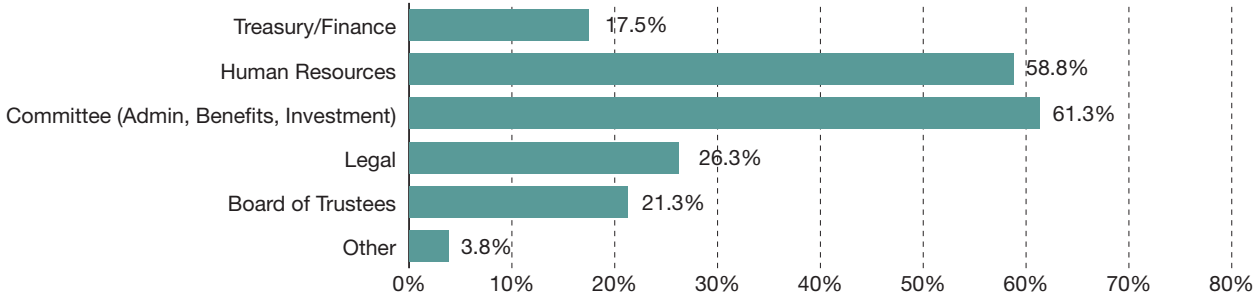
Throughout this survey, charts may not sum to 100% due to rounding.

Plan Oversight and Decision Making

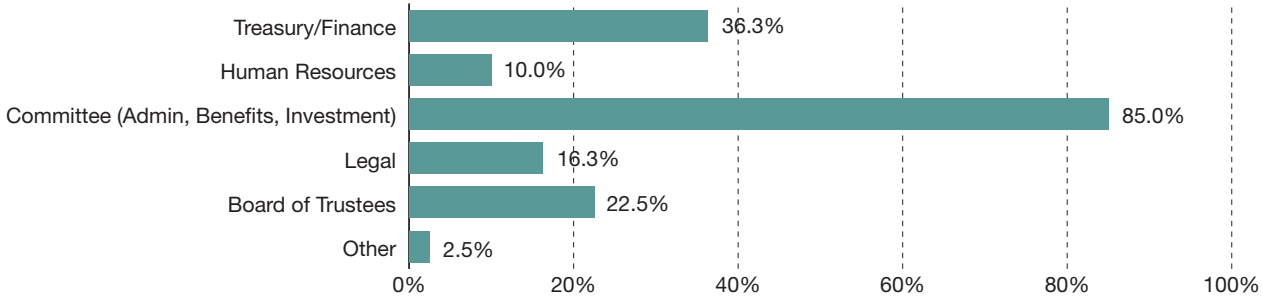
For DC plans, administrative decisions most frequently reside with a committee comprised of administrative, benefit and investment professionals (61.3%) or human resources (58.8%). By contrast, investment decisions are generally made by a committee (85.0%), and less so by only treasury/finance (36.3%).

Quarterly investment committee meetings remain the norm, with three in four (77.5%) respondents holding meetings at this frequency. Last year during the worst market collapse since the Great Depression, 76% of plan sponsors reported they increased the frequency of investment committee meetings. In 2009, only one in five (20.3%) increased meetings. Just under two-thirds (64.6%) engaged the services of an investment consultant—a considerable drop from 2008 (76.5%). Plans with $200 to $500 million in assets (85.7%) are most likely to use a consultant.

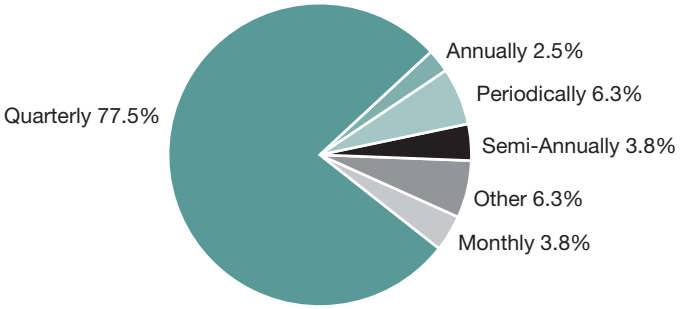
Which part of your organization makes *administrative* decisions for your DC plan?[A]



Which part of your organization makes *investment* decisions for your DC Plan?[A]



What is the frequency of investment committee meetings at your organization?



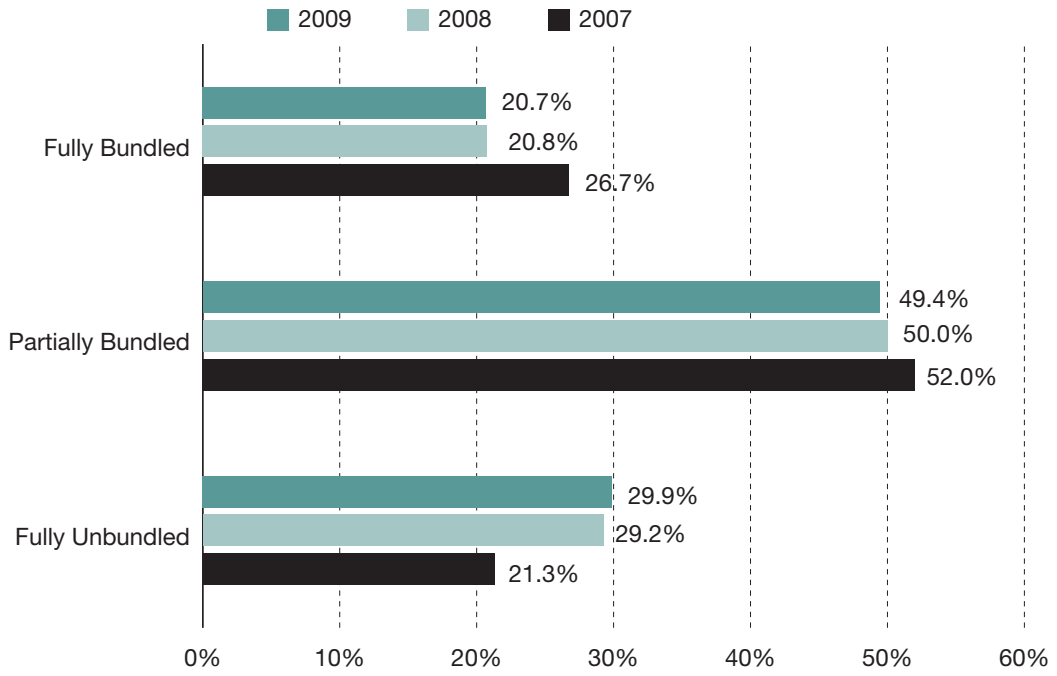
[A] Multiple responses were allowed.

Use of Bundled Arrangements

The recent trend in the unbundling of DC plans has remained flat year over year, with virtually the same percentage of plan sponsors offering fully bundled, partially bundled and unbundled plans in 2009 versus 2008. Conversely, from 2007 to 2008, unbundling of DC plans made significant strides—plan sponsors offering fully unbundled plans jumped from 21.3% to 29.2%, while fully bundled plans declined from 26.7% to 20.8%.

The drop-off in the movement toward unbundling may be partly attributable to the fallout from the 2008-2009 market crisis; many plan sponsors were too busy shoring up their retirement plans in the face of massive market declines to focus on strategic initiatives such as unbundling. However, the unbundling trend is likely to continue in light of upcoming fee disclosure regulations and ongoing legislative scrutiny of DC plan fees since unbundled plans offer a high level of fee transparency. For large plans, unbundling can also result in reduced costs to plan participants, more equitable fee payment and increased investment flexibility.

Describe your plan structure:



Fully Bundled = the recordkeeper and trustee are the same, and all of the investment funds are managed by the recordkeeper.

Partially Bundled = the recordkeeper and trustee are the same, but not all of the funds are managed by the recordkeeper.

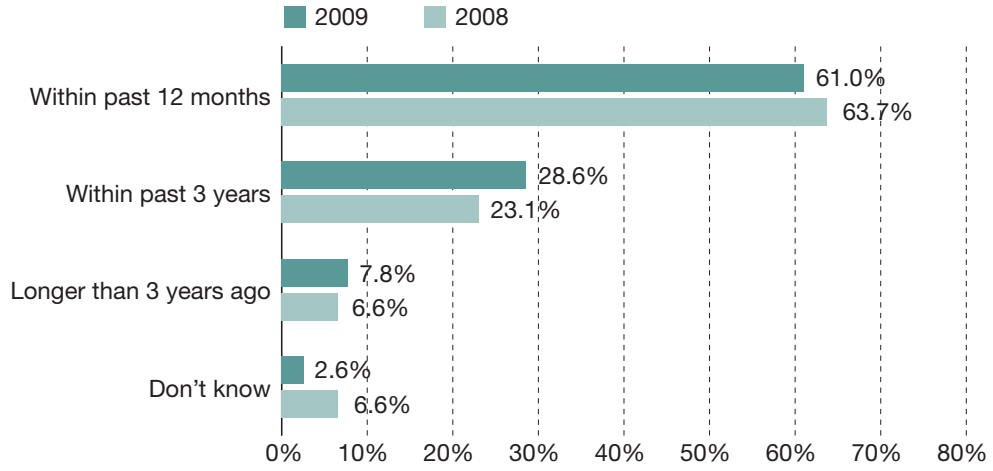
Fully Unbundled = the recordkeeper and trustee are independent, and none of the investment funds are managed by the recordkeeper.

Investment Policy Statement, Compliance and Fiduciary Positioning

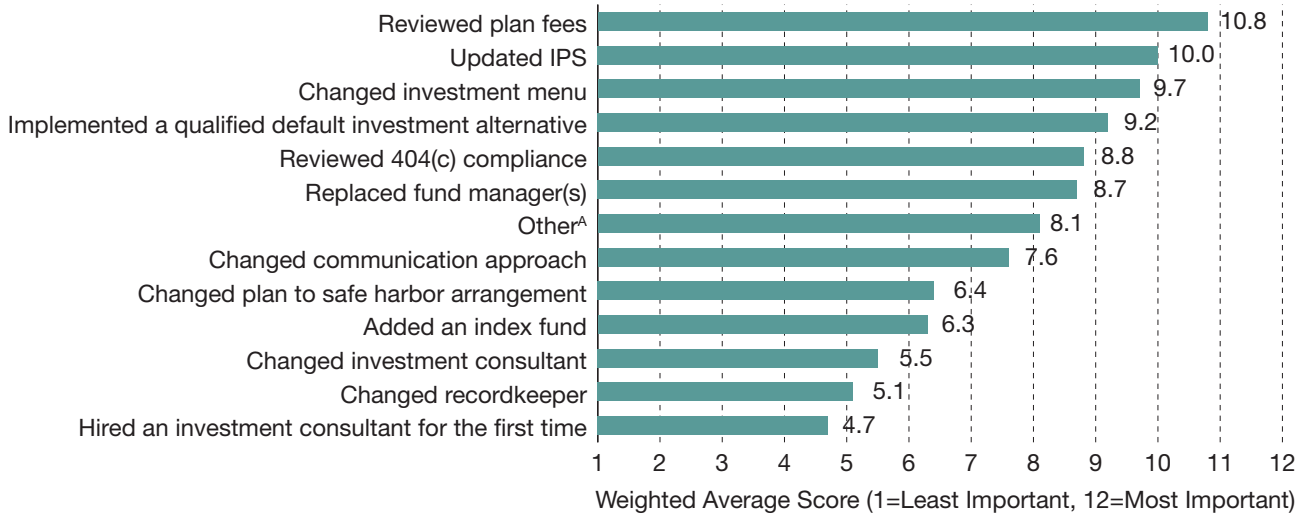
Most DC plan sponsors (86.5%) maintain an investment policy statement (IPS). IPS's are highly prevalent in 401(k) plans at 90.6% in 2009. Sixty-one percent of plan sponsors have reviewed their investment policy statement within the past 12 months and another one-quarter (28.6%) reviewed it within the past three years. However, one in 10 (10.4%) plan sponsors either have not reviewed their investment policy statement within the past three years or do not know when they last reviewed it, down slightly from 2008. Just under three-quarters (72.2%) of plan sponsors report that their plans are designed to be 404(c) compliant, while only 7.6% say they are not. As in 2008, the remaining one-fifth of sponsors did not know whether or not their plans are compliant, undoubtedly reflecting the complexities of 404(c) adherence. Industry experts have asserted that plans that are designed to be 404(c) compliant may actually suffer material compliance holes.

When asked to rank the most important steps they have taken to improve the fiduciary positioning of their DC plan within the past 12 months, plan sponsors cited reviewing plan fees as number one, followed by updating the IPS. Meanwhile, reviewing 404(c) compliance ranked fifth after fund lineup and default investment changes.

When was the last time the Investment Policy Statement was updated?



Rank the most important steps that you have taken to improve the fiduciary positioning of your DC plan within the past 12 months.

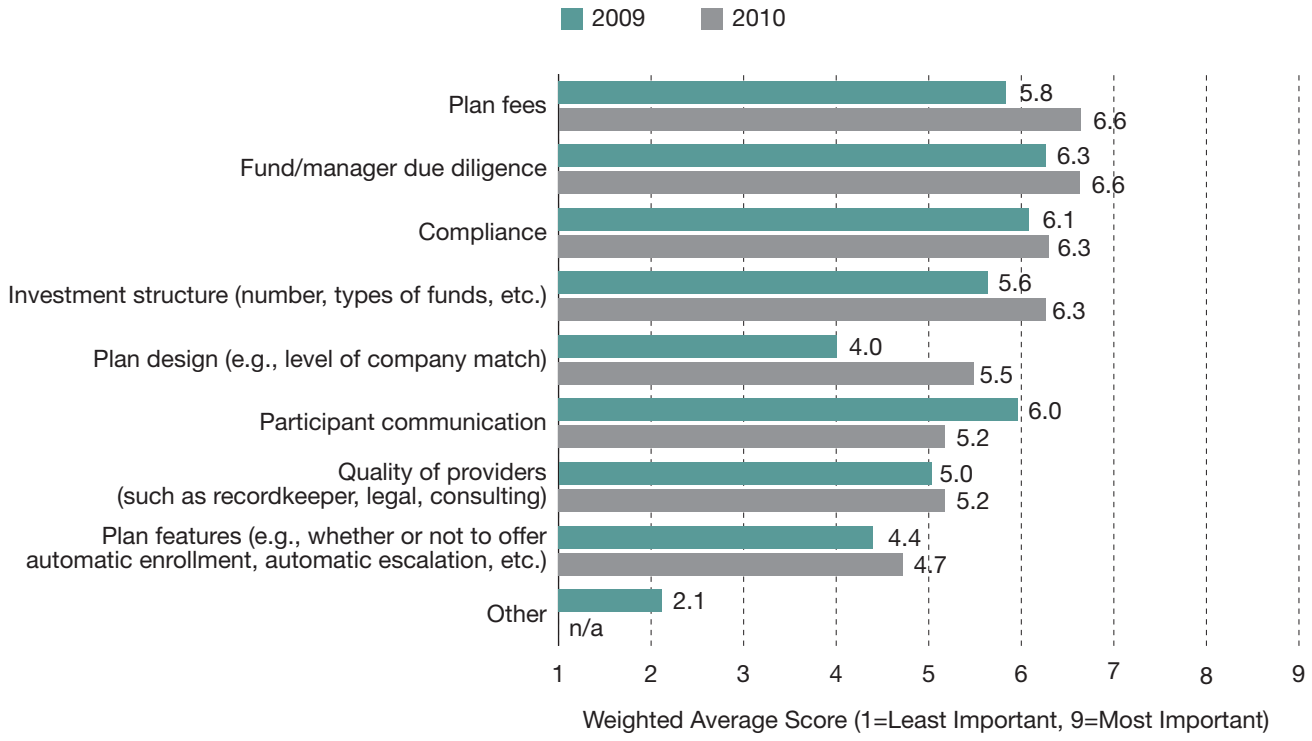


[A] Other includes: formed an investment committee, implemented limits on company stock, disclosed fees, and implemented a self-directed brokerage account.

Areas of Plan Sponsor Focus in 2010

Following the market collapse, fund/manager due diligence ranked as the number one area of focus for 2009. However, going into 2010, strategic initiatives, such as plan fees, investment structure and plan design, have risen in importance. Fund/manager due diligence remains a high priority, ranking inline with plan fees, followed by compliance and investment structure. Participant communication—which ranked third in 2009—has dropped out of the top five for 2010, undoubtedly due to improved market stability and a reduced need to communicate about the markets.

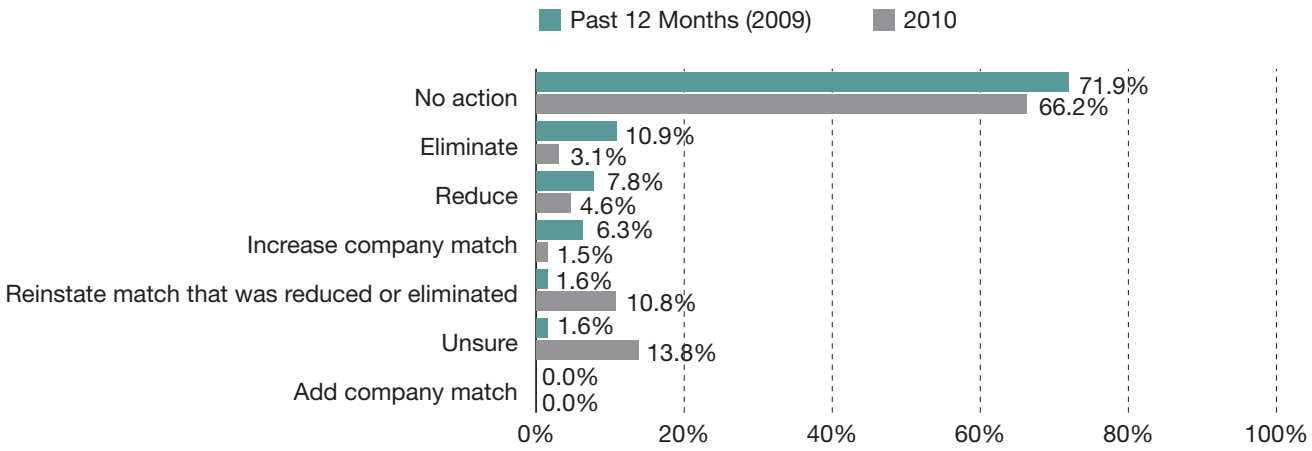
What were/are likely to be your primary areas of focus?



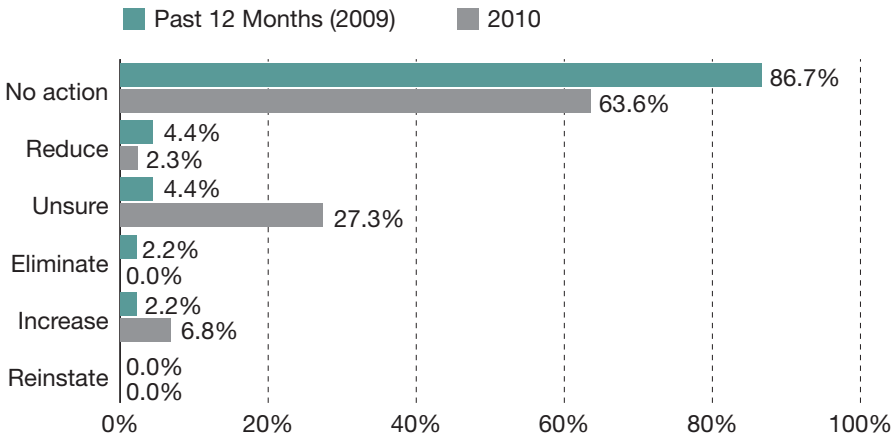
Areas of Plan Sponsor Focus in 2010 (continued)

Notably, seven in 10 plan sponsors made no changes to their company match in 2009. Nearly one in five (18.7%) reduced or eliminated it over the same time period and another nearly 8% intend to do so in 2010. However, among those that eliminated or reduced the match, more than half (58%) expect to reinstate the match next year. Nearly 14% are not sure what the fate of the match will be in 2010, down from about 20% who were unsure when asked this question in 2008. Meanwhile, 27.3% are currently unsure about the future of their plan's non-matching contribution.

What steps have you taken this year, or are you likely to take, with respect to the company match?



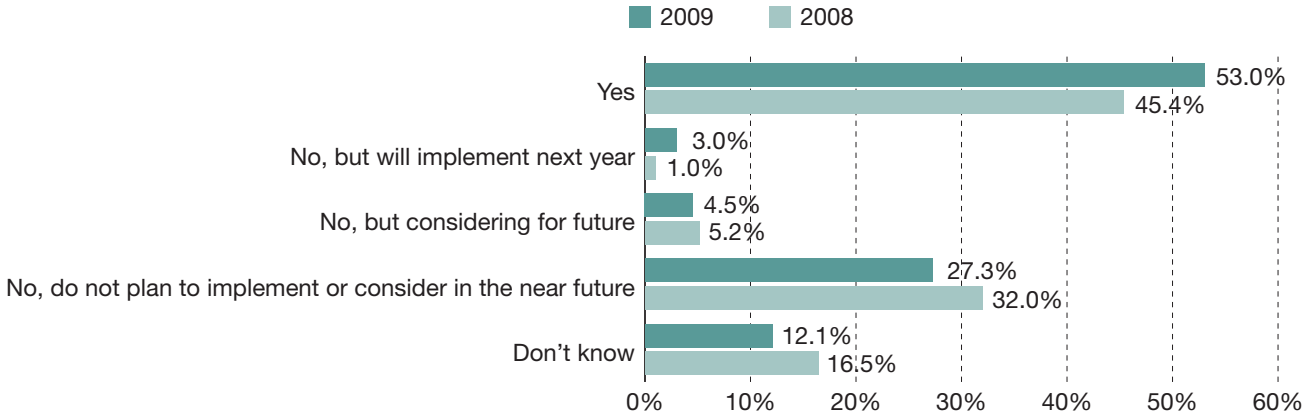
What steps have you taken this year, or are you likely to take, with respect to the company non-matching contribution?



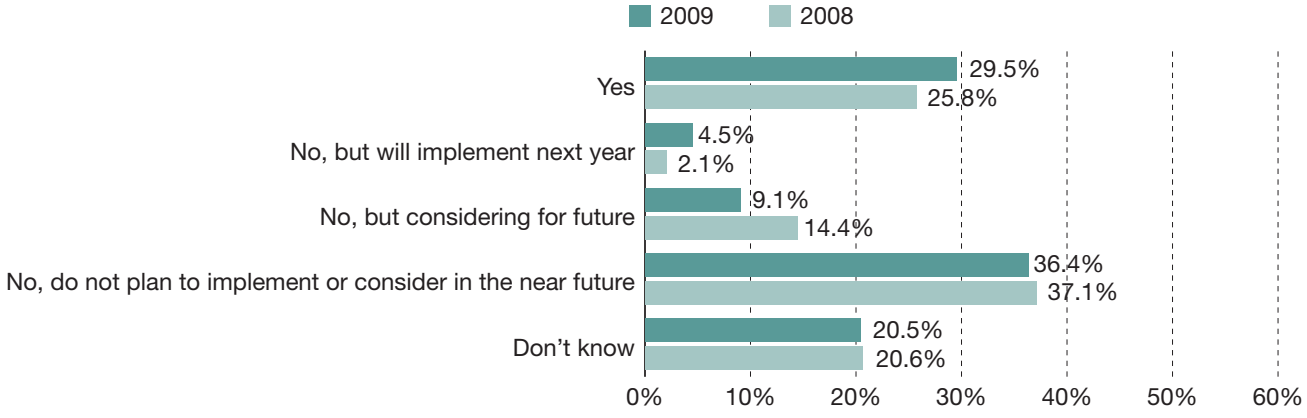
Safe Harbor Utilization

More than half (53%) of plans now conform to the traditional non-discrimination testing safe harbor, up from 45.4% in 2008. Meanwhile, 29.5% conform to the automatic enrollment non-discrimination testing safe harbor (qualified automatic contribution arrangement, or QACA), up from 25.8% in 2008. These numbers are remarkable, given that both safe harbors require either matching or non-matching company contributions, which were on the decline last year. Sixteen percent of plans surveyed offer both safe harbors.

Does your DC plan conform to the traditional non-discrimination testing safe harbor (the pre-2006 Pension Protection Act safe harbor)?



Does your company plan conform to the non-discrimination testing safe harbor for automatic enrollment as defined under the Pension Protection Act?

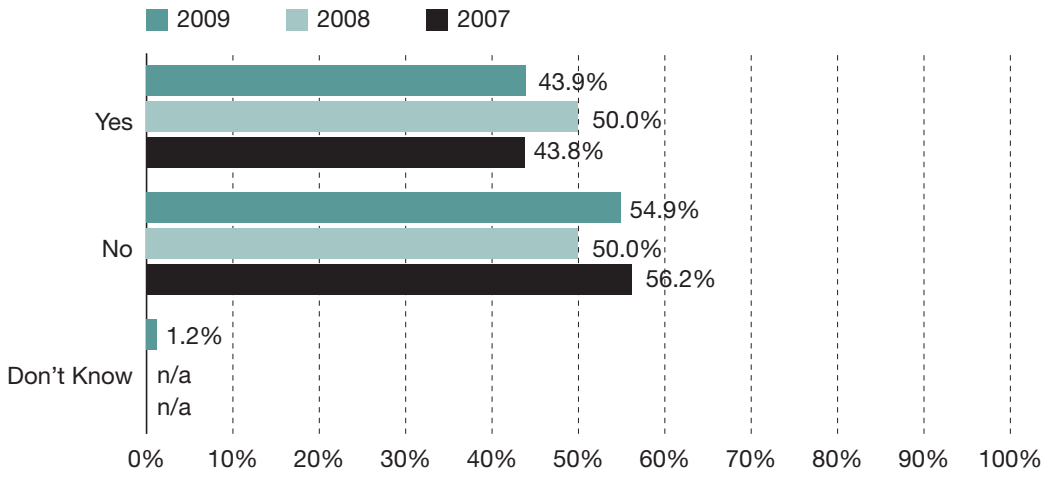


Automated Plan Features

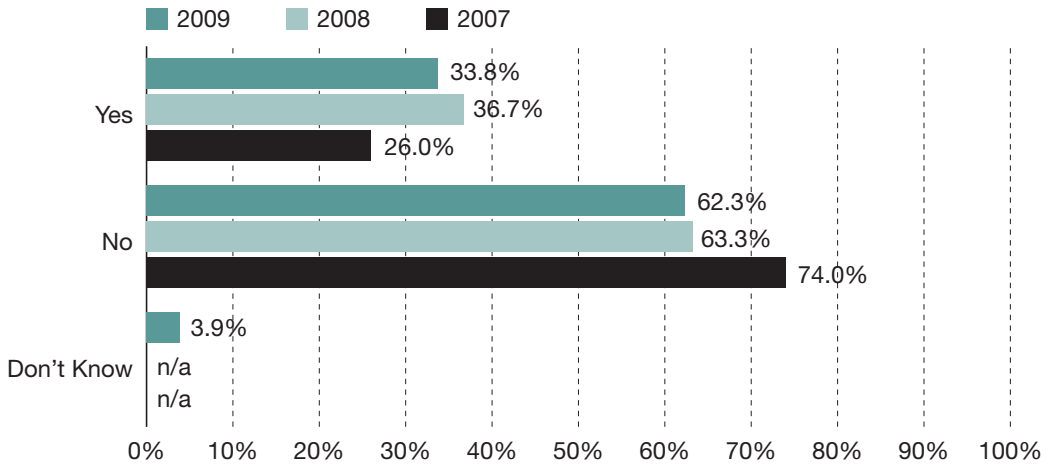
Adoption of auto features has plateaued recently. In 2009, just under half (43.9%) of the plans offer automatic enrollment. This figure has hovered between 44% and 50% since 2007, indicating little additional appetite for this feature. Likewise, the proportion of plans offering automatic escalation has stagnated at about one-third (33.8%) over the past several years. Even the few plan sponsors interested in offering auto features in 2009 were undoubtedly daunted by the volatile market and the uncertain fate of their ability to make company contributions. In 2010, 45.5% of plan sponsors indicate they are likely to offer automatic enrollment and 33.8% are likely to offer automatic contribution escalation.

The average automatic enrollment contribution default rate rose from 3% in 2008 to 3.6% in 2009. However, this remains low relative to the rate "prescribed" under the qualified automatic contribution arrangement (QACA) regulations. Under QACA, the minimum automatic employee deferral percentage must ultimately be 6% in order for the plan to avoid non-discrimination testing requirements. Of course, non-QACA plans are not required to adhere to this regulation. Interestingly, the average cap on the automatic contribution rate increase is inline with QACA's required 10% cap, with reported contribution escalation caps ranging from as low as 4% to as high as 25%.

Does your DC plan currently offer automatic enrollment?



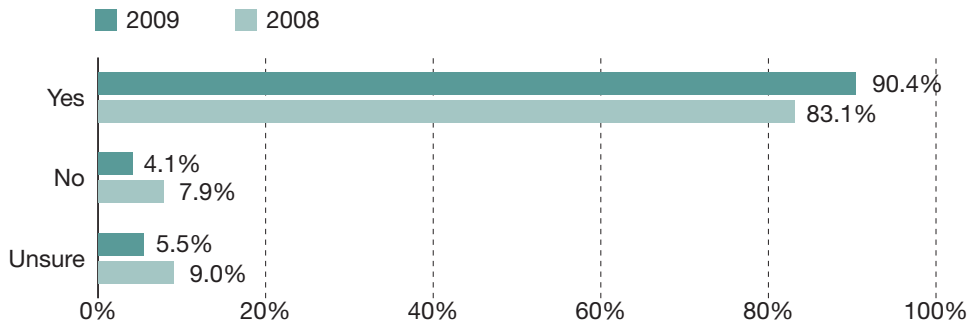
Does your DC plan currently offer automatic escalation?



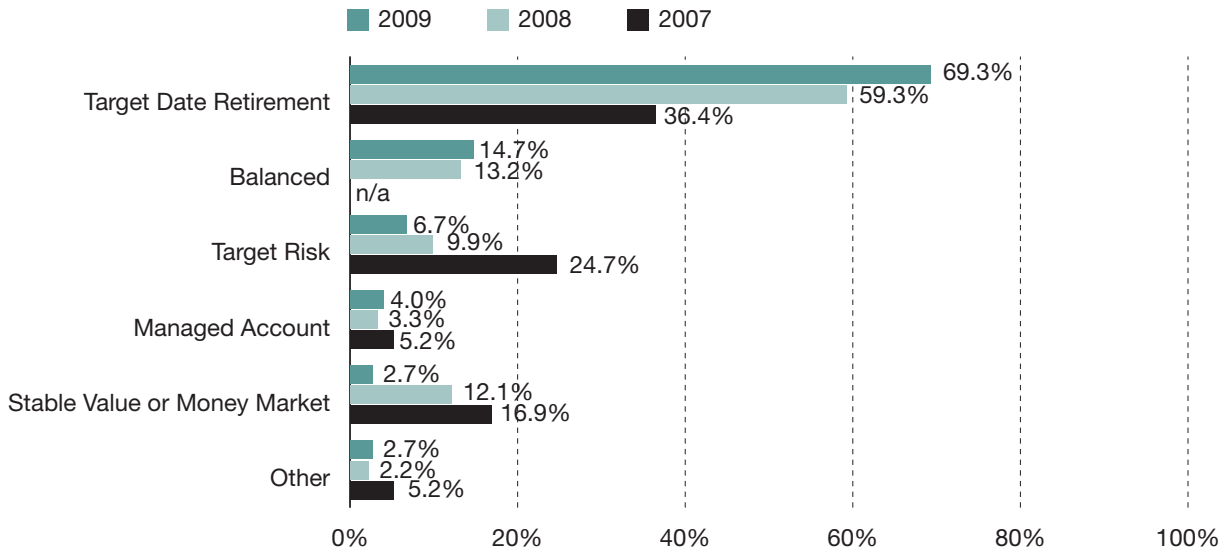
Default Investments

Most DC plans now have a qualified default investment alternative (QDIA), and target date funds are the clear QDIA of choice. In 2009, 69.3% of plan sponsors reported that their default is a target date fund, up from 59.3% in 2008. This notable increase follows an arguably tough year for target date funds in 2008, when their divergent returns drew regulatory and legislative scrutiny. Nonetheless, much of the growth in target date funds as a default comes from plan sponsors shifting away from defaulting to money market or stable value funds—which do not qualify as QDIAs. This speaks to the strong appeal of the ERISA 404(c) safe harbor, gained through the adherence to QDIA regulations. Additionally, some of the growth in target date funds as defaults is also due to movement away from target risk funds (also QDIAs). In other words, despite a rough 2008, plan sponsors continue to embrace target date funds.

Is your DC plan's default investment fund a Qualified Default Investment Alternative (QDIA)?



What is your current investment alternative for non-participant directed monies?



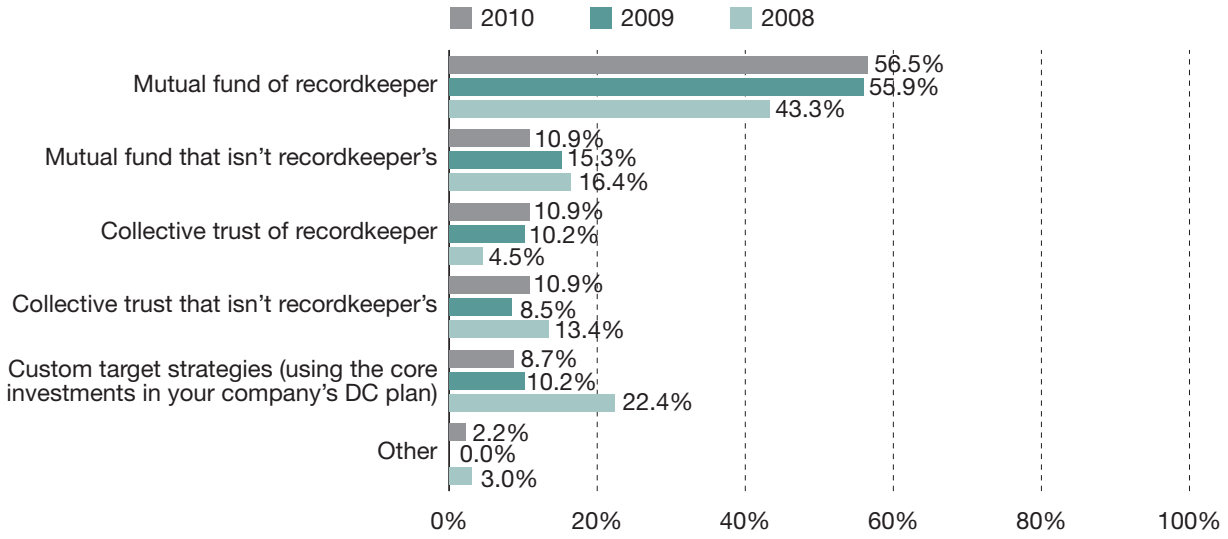
Target Date Funds

The majority (55.9%) of DC plans use the proprietary target date funds of their recordkeeper—a figure that shows no sign of changing next year. However, as in prior years, the fact that the target date funds are proprietary to the recordkeeper ranks low in the plan sponsors' list of criteria for selection. In contrast, portfolio construction and performance continue to rank high in selection criteria, pointing to a potential disconnect between target date fund selection and the actual target date fund selection process. It is difficult to believe that proprietary target date funds' portfolio construction and performance are so consistently superior to that of other available target date funds.

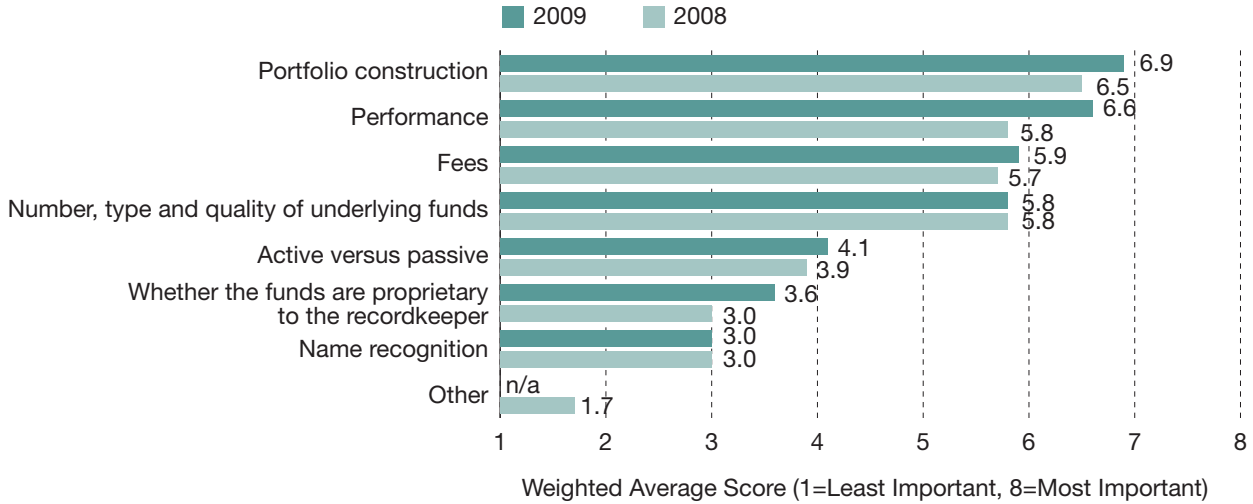
Fees rank third in importance of selection and retention criteria, which may actually explain the high use of proprietary funds. Recordkeepers often provide advantageous pricing to plan sponsors that use the "house" target date funds in their plan.

A mix of active and passive target date funds is most prevalent (37.3%), but not by much. About one-third (35.3%) of plans offer active target date funds, while over one-quarter (27.5%) offer passive target date funds.

What target date fund approach is being/will be used?



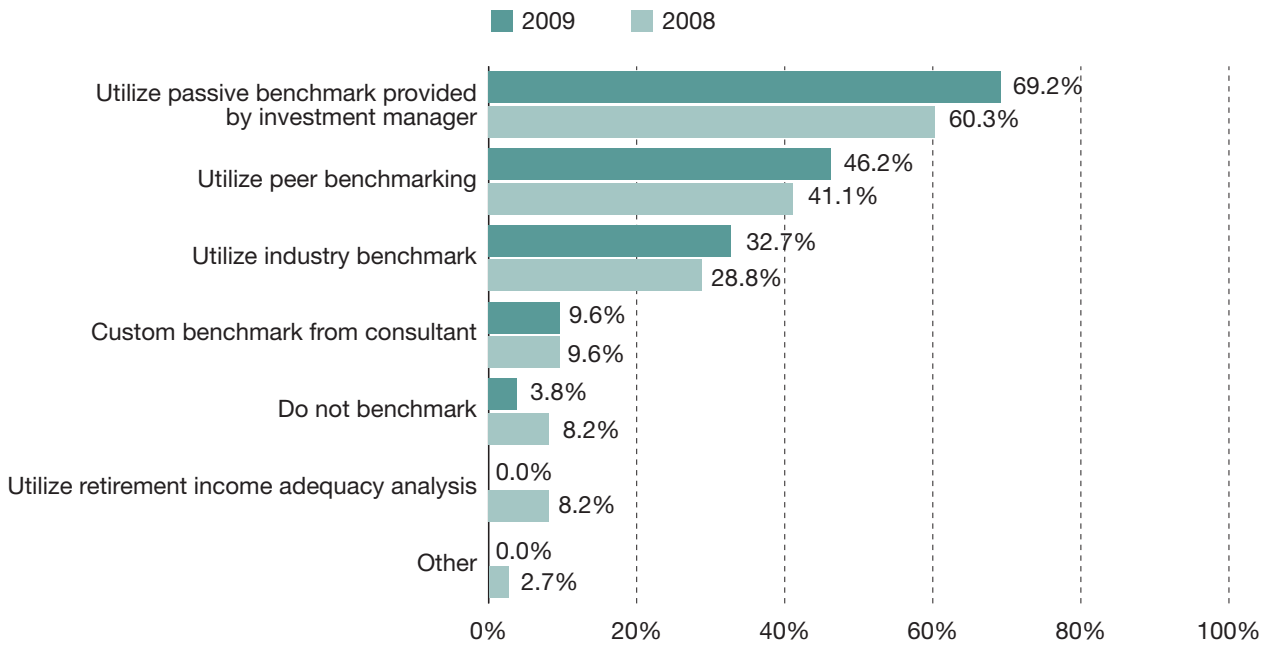
What are the most important criteria for selecting or retaining target retirement date funds?



The most common benchmark for target date fund performance remains the passive benchmark of the investment manager (69.2%). Use of peer benchmarking (46.2%) and industry benchmarks (32.7%) are on the rise.

For 2010, plan sponsors most commonly expect to change communications about their target date funds and the share class of these offerings (both 28.6%).

How do you monitor target retirement date funds?[A]



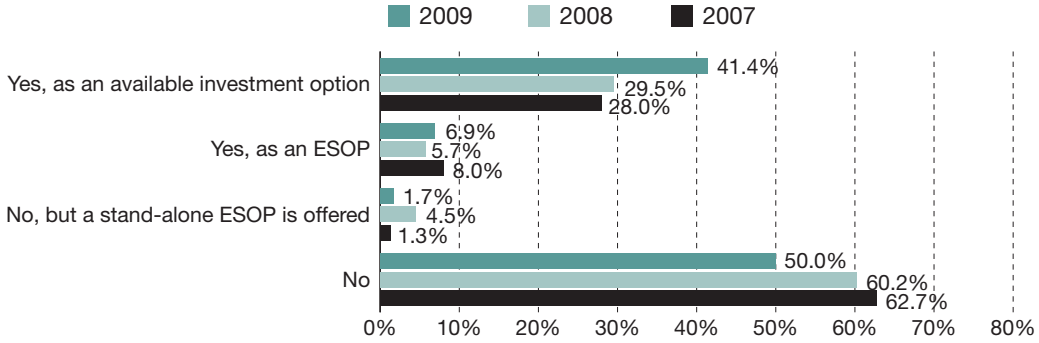
[A] Multiple responses were allowed.

Company Stock

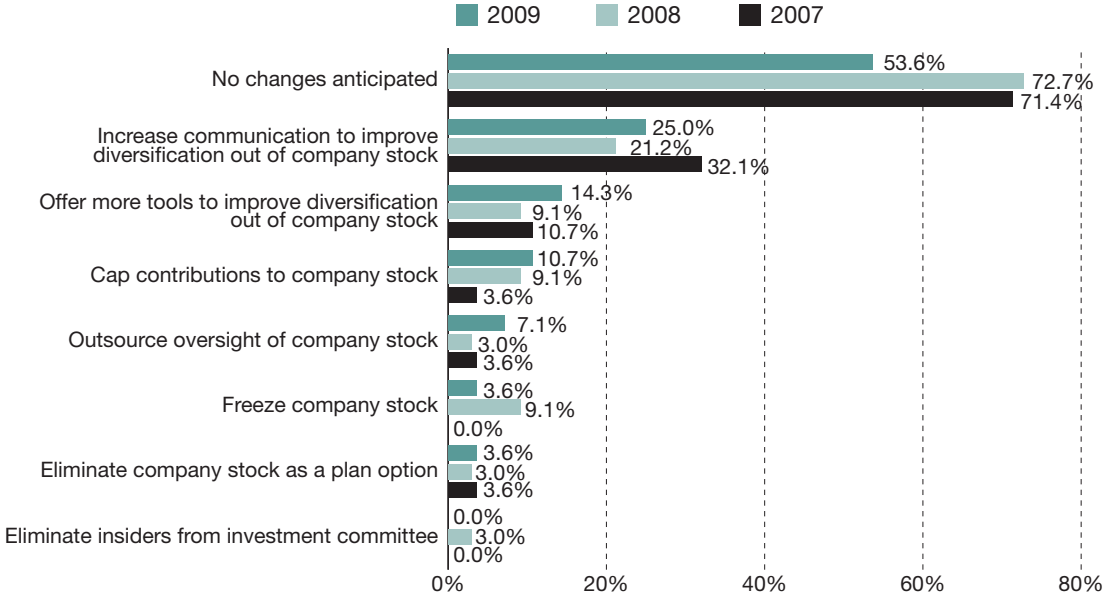
In 2009, 41.4% of plan sponsors offered company stock as an investment option to DC participants. This is higher than in previous years, but likely represents a difference in sample as opposed to an increase in plans offering this option. There is little anecdotal evidence that plan sponsors are actively adding company stock funds to DC plans.

More plan sponsors anticipate making a change to company stock in 2010 than in previous surveys (46.4%). As in prior years, the most commonly cited changes are increasing communication to improve diversification out of company stock (25%) and offering more diversification tools (14.3%). Eliminating insiders from the investment committee and freezing or eliminating company stock remain among the least popular changes.

Is company stock offered in the plan?



What changes do you anticipate with respect to company stock in the next year?

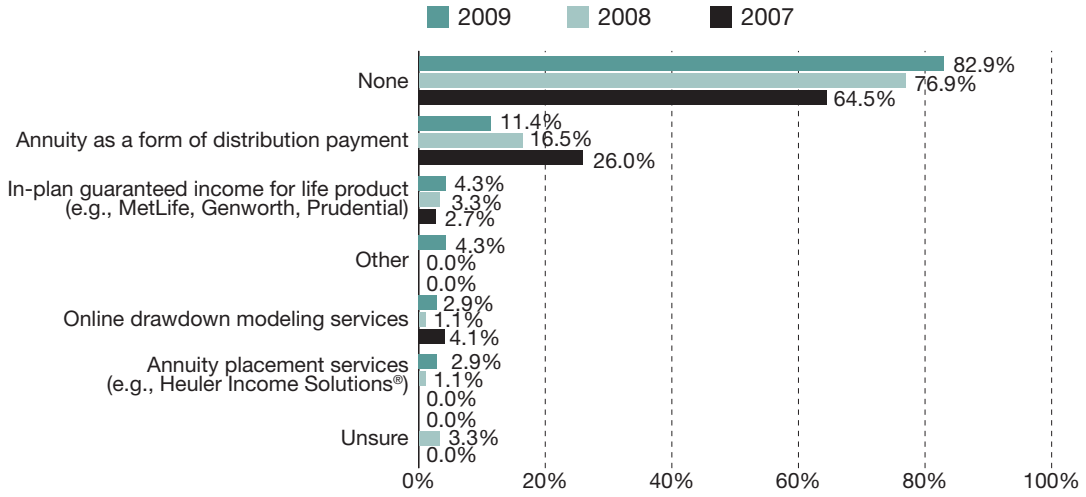


Retirement Income Solutions

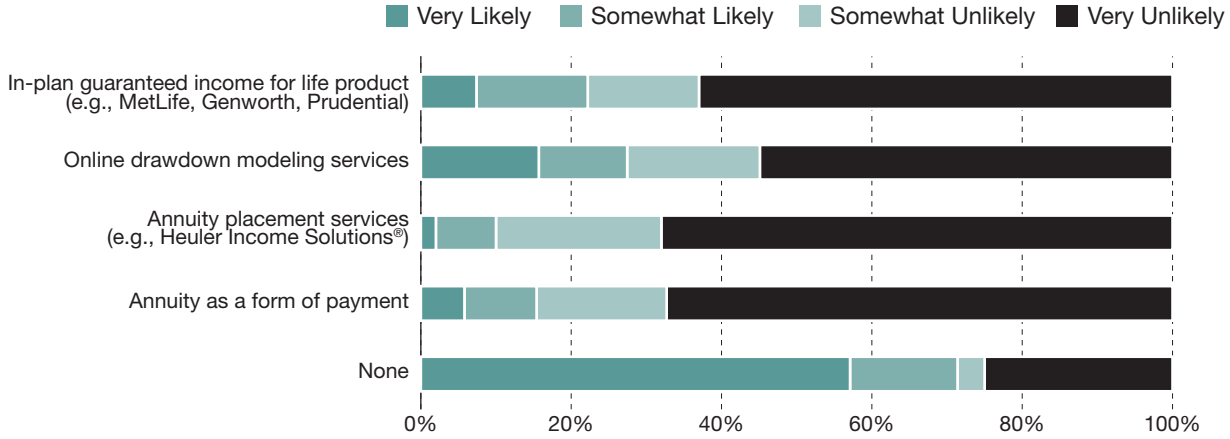
Few plans offer retirement income solutions, including annuities or drawdown services. Indeed, certain retirement income options, such as annuities as a form of distribution payment, significantly declined in prevalence in the past few years. Declines are noted despite regulatory support—with the passage of the 2006 Pension Protection Act, annuities in DC plans are no longer required to be the safest available.

Additionally, adoption of in-plan annuities—while garnering interest from some plan sponsors—remains low at 4.3% in 2009. Going forward, online drawdown modeling services, which have a low level of fiduciary implications, are most likely to be added by plan sponsors in 2010 (16%). As reported last year, only about 7% of plan sponsors are very likely to add in-plan annuities.

What form of income for life product does your plan offer to employees?



Indicate your company's likelihood of offering the following guaranteed income for life products to employees in the next year:

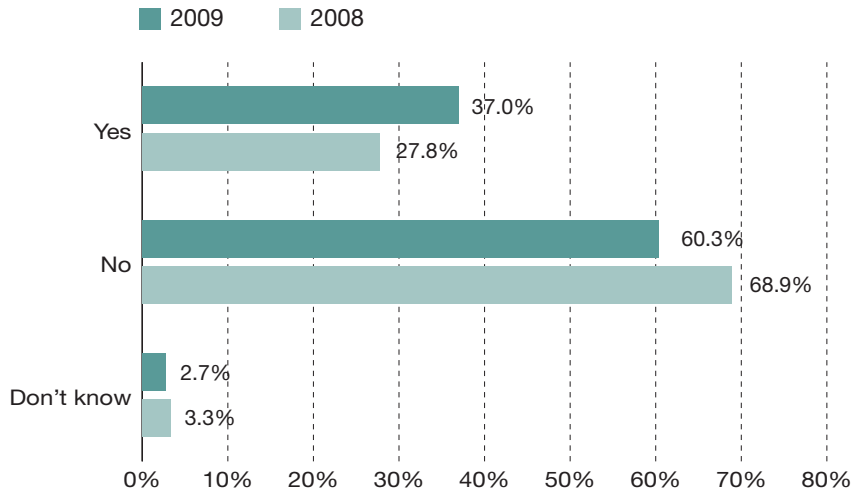


Roth Contributions

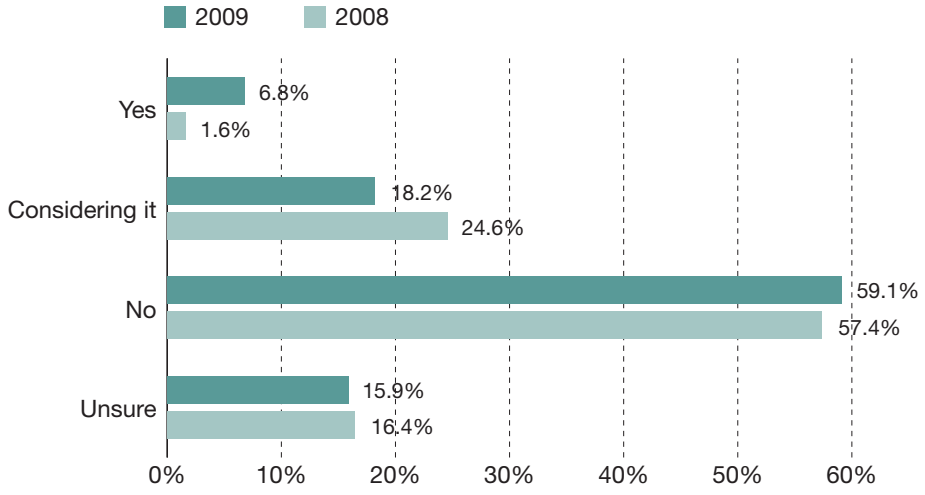
While plan sponsors expressed only a modest level of interest in adding Roth contributions in 2008 (about one-quarter were considering it and less than 2% intended to add it), the use of this option across participants grew materially from 27.8% in 2008 to 37% in 2009. Increased use may be due to participant demand, as Roth programs in general have gained attention recently with the upcoming changes in conversion rules for Roth.[A]

Another 6.8% of plan sponsors intend to add Roth contributions in 2010, and about one in five (18.2%) are considering it.

Does your DC plan allow for Roth contributions?



Do you intend to offer Roth contributions for your DC plan in the next year?

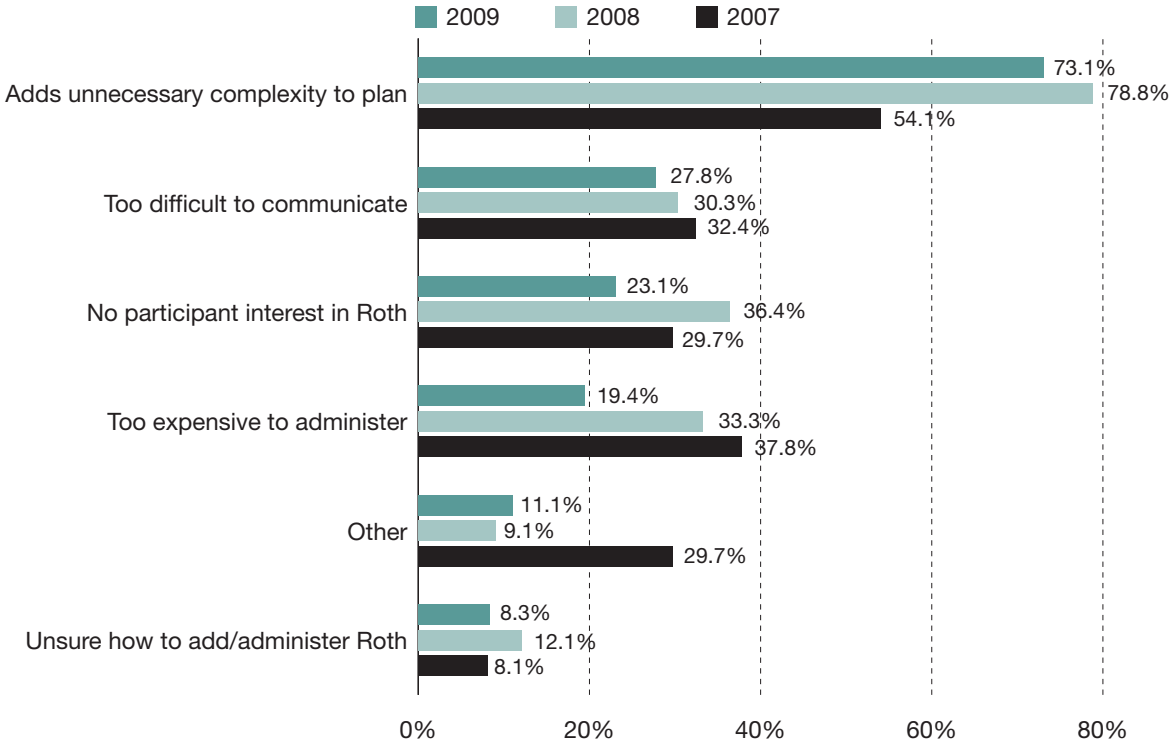


[A] Starting in 2010, taxpayers with modified adjusted gross income of more than $100,000 will be allowed to convert a traditional IRA to Roth IRA.

Roth Contributions (continued)

The foremost reason given by plan sponsors for not offering Roth contributions is concern about adding unnecessary complexity to the plan (73.1%). This concern has grown in recent years.

If no, please give reason(s) why a Roth option won't be offered?[A]



[A] Multiple responses were allowed.

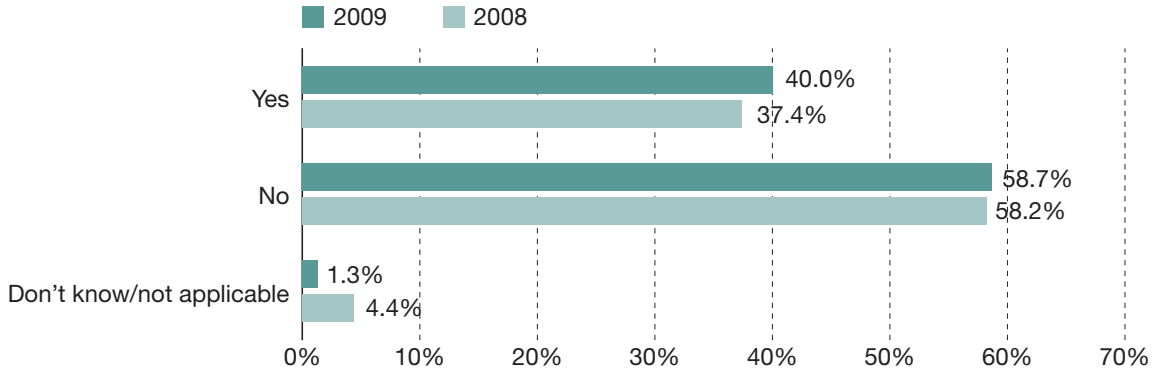
Investment Advice

The proportion of plans offering online investment advice has marginally increased to 40%. Of the plan sponsors that currently do not offer online investment advice, one in 10 were very likely to add it in 2010. This low level is not surprising given the regulatory uncertainty that surrounds this topic. Final Department of Labor regulations for the 2006 PPA have not been passed, and some legislators question the scope of investment advice permitted by originally proposed regulations.

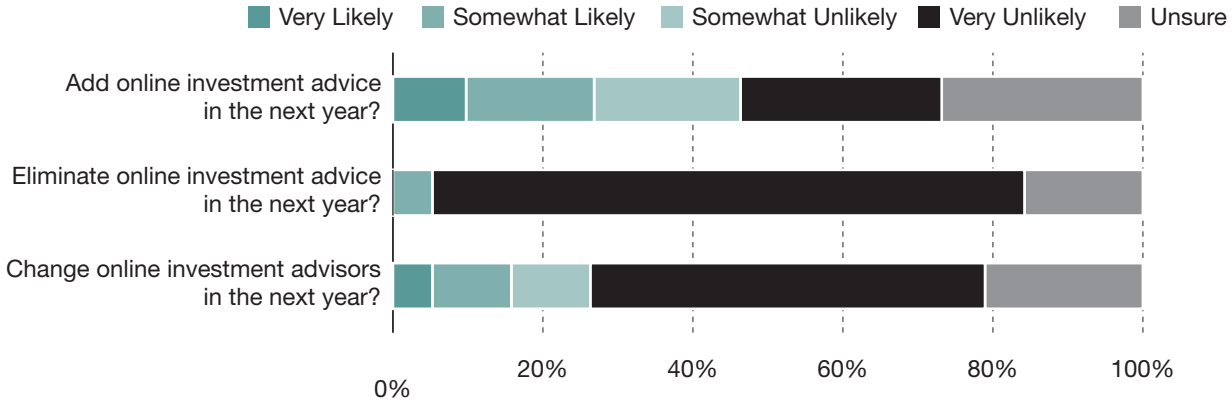
Among those that offer online investment advice, only 20% are very satisfied with participant utilization and 56.7% are somewhat satisfied. Despite a lack of complete satisfaction with online advice, none of the respondents expect to eliminate online advice in 2010 and only 5.3% expect to change online advice providers. Changing providers can be challenging, as often only one advice provider is offered through a given recordkeeper. In terms of providers, Financial Engines is the most commonly used online advice provider, cited by more than twice as many plan sponsors as its nearest competitor, Morningstar.

Plans sponsors that do not offer online investment advice frequently cite low participant demand/low potential utilization and uncertainty about the regulatory environment.

Do you offer online investment advice today?



How likely are you to:



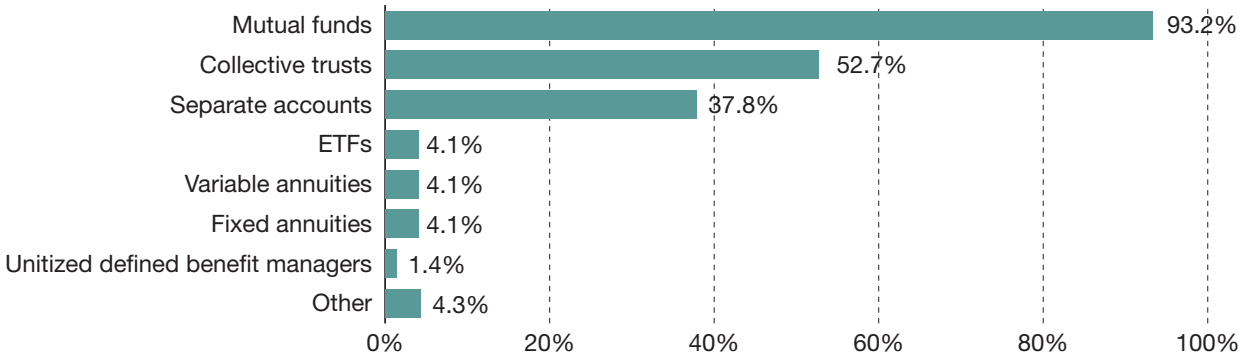
Investment Menu

DC plans generally offer a mix of mutual funds, collective trusts and separate accounts in their fund lineup. Mutual funds dominate, with 93.2% of plan sponsors citing them as an available investment vehicle. However, more than half of respondents also use collective trusts (often a stable value fund) and over one-third (37.8%) use separate accounts. While there has been considerable industry buzz about exchange-traded funds, only 4.1% of plans offer these vehicles, which are generally not well-suited to large DC plans.

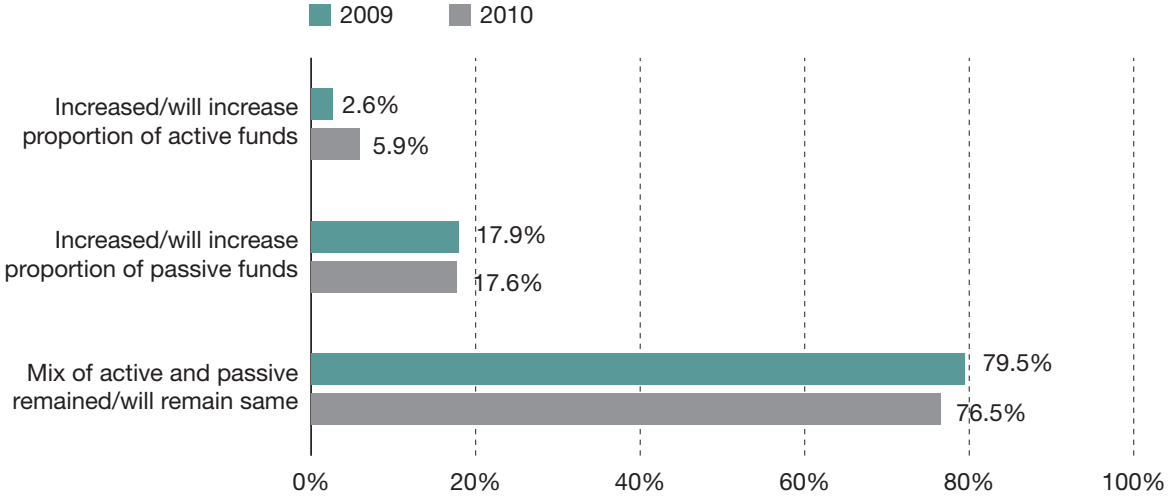
The survey also shows that larger plans are less likely to offer mutual funds and more likely to offer separate accounts.

The vast majority (87.7%) of plan sponsors describe their fund menu as a mix of active and passive options, with 4.1% of plans offering passive-only and 8.2% offering active-only menus. At the same time, 17.9% of plan sponsors increased the number of passive funds in their plan's menu in 2009 and another 17.6% expect to in 2010. This may reflect pressure on plan sponsors to reduce plan fees and their perception that index funds are easier to monitor within the plan.

Are the following options offered?[A]



How did the plan's investment menu change in 2009/will change in 2010?

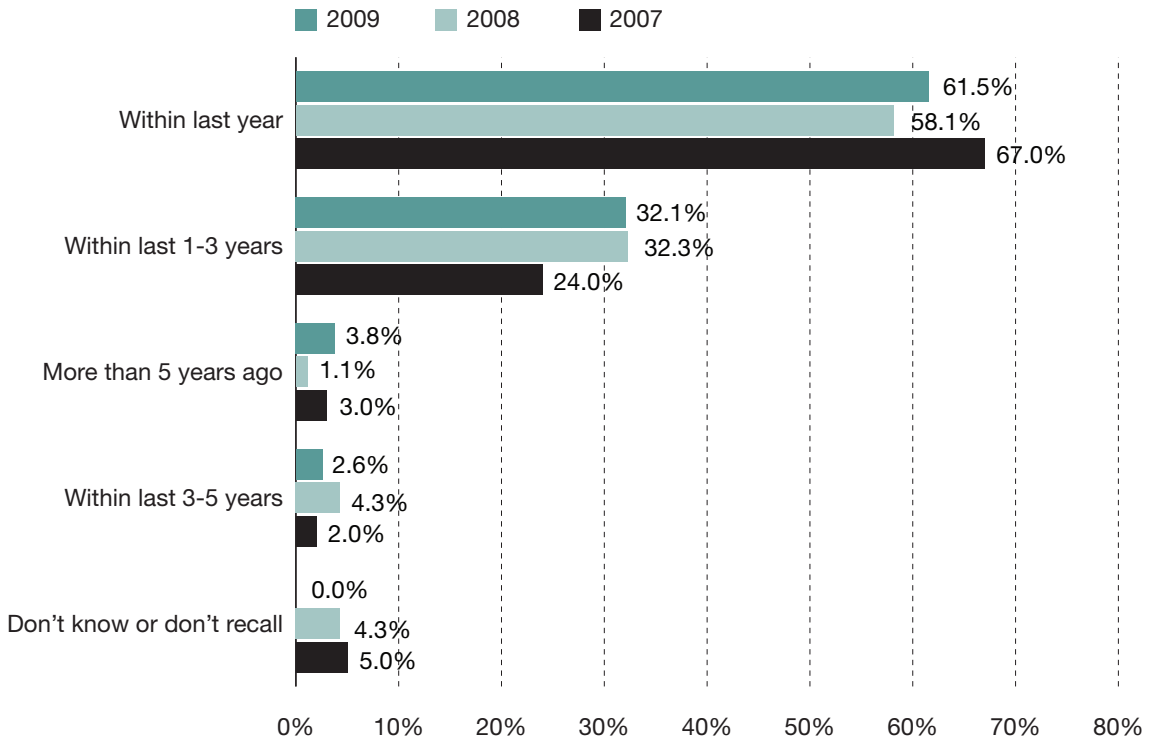


[A] Multiple responses were allowed.

Investment Structure

Most plan sponsors allow no more than three years to pass before conducting an investment structure analysis. In 2009, nearly two-thirds (61.5%) of plan sponsors conducted an investment structure evaluation, up slightly from last year. Given plan sponsors' single-minded focus on managing underperforming funds early in 2009, the uptick in strategic activity of investment structure evaluation is notable, but did not approach 2007 levels.

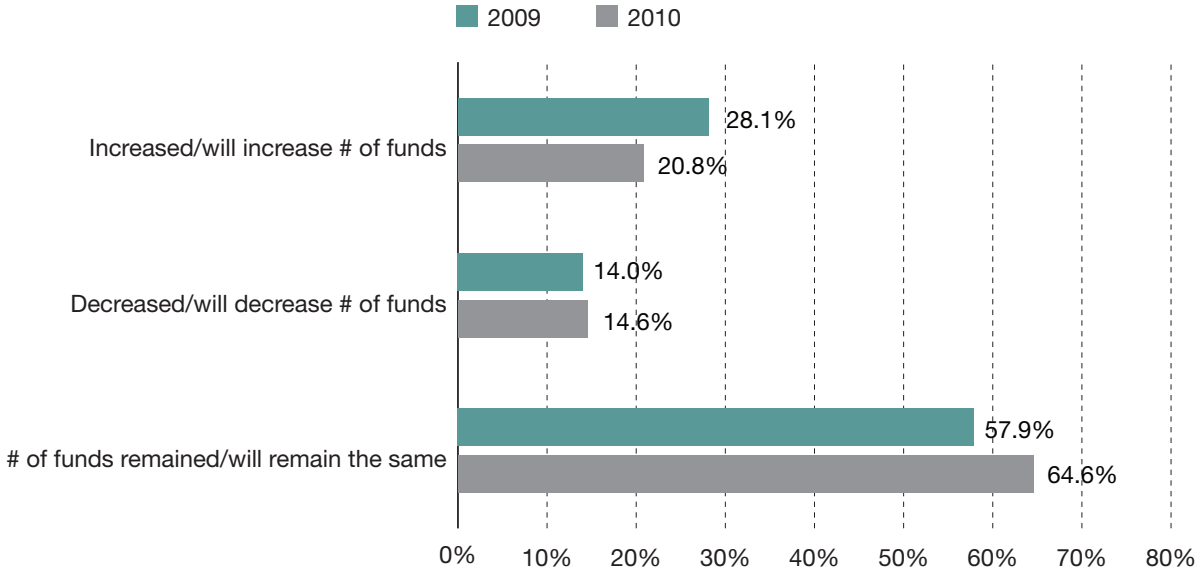
When was the last time your organization conducted an investment structure evaluation to determine gaps/overlaps in investment offerings?



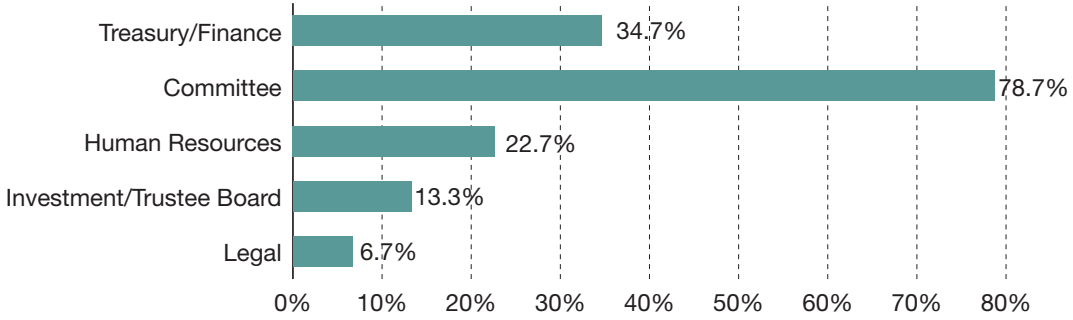
In redesigning investment structure in 2009, more plan sponsors increased the number of funds (28.1%) than decreased them (14.0%). This is despite the oft-stated objective of streamlining the investment fund lineup. Reflecting inflation concerns, real return/TIPS were the most common fund addition. Target date funds came in second due to their popularity despite the stresses of 2008, along with domestic fixed income, reflecting plan sponsors' interest in providing additional diversification opportunities for investment-risk-averse participants. For 2010, plan sponsors expecting to add funds once again most anticipate selecting real return/TIPS followed by target date funds. Interestingly, a number of the plan sponsors that are increasing funds in 2010 report that they will be implementing a new fund lineup, which is usually the result of switching recordkeepers.

Small/mid cap equity was the most commonly eliminated fund in 2009. This likely reflects the extraordinarily poor performance of active small/mid cap managers in the third quarter of 2008. In 2010, 17.6% of plan sponsors expect to eliminate large cap domestic equity—more than any other asset class. When funds are eliminated, the most common mapping method is to direct the assets to the most similar fund based on matching the risk level of the existing fund with the new fund (89.3%). Only 3.6% map to the default fund; the remaining 7.1% are unsure. Only one-third (34.7%) of plan sponsors rely on treasury/finance for its investment structure evaluation decision, while three-quarters (78.7%) empower a committee.

How did the plan's investment menu change in 2009/will change in 2010?



Who were the primary decision makers in the investment structure evaluation?[A]

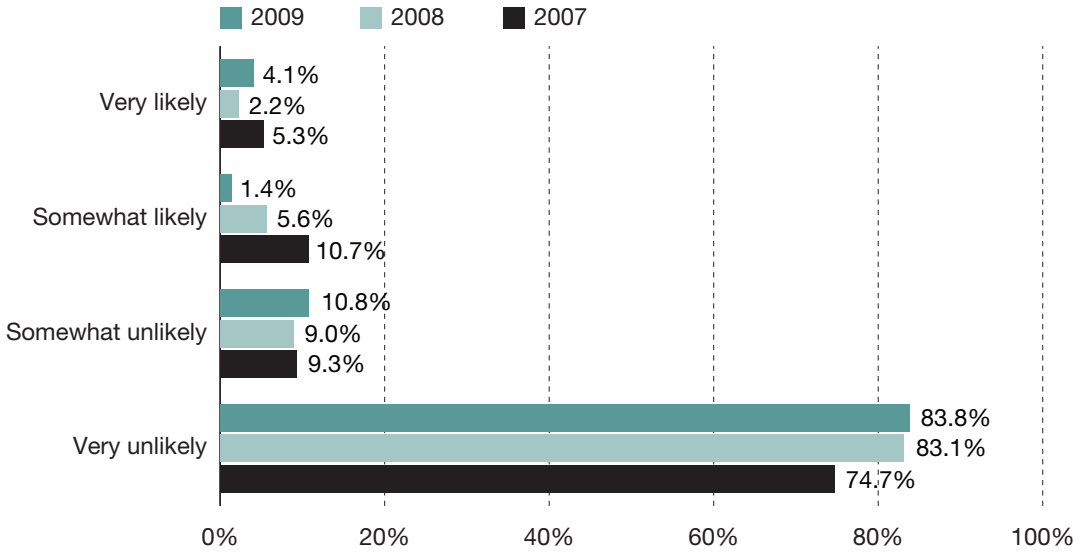


[A] Multiple responses were allowed.

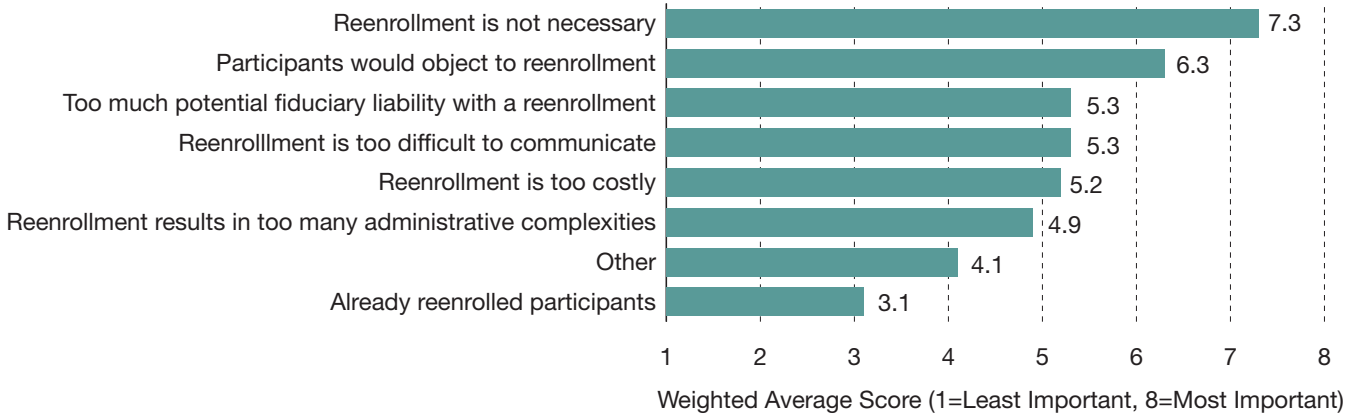
Reenrollment

Plan sponsors are slightly more likely to reenroll participants in 2010 than they said they were a year ago. Reenrollment is defined here as requiring all participants in the plan to make new fund selections or else be directed into the default investment option. While 4.1% are very likely to reenroll participants in 2010, only 2.2% indicated they were very likely the prior year. The most common reasons for reenrolling participants are changes to the fund lineup (60%) followed by a new recordkeeper (20%). Top reasons plan sponsors do not reenroll participants are that it is viewed as unnecessary or because participants would object. Some cite concerns that this is a questionable fiduciary practice.

Do you plan to engage in a "reenrollment" in the next year (requiring all participants in the plan to make new fund selections or else be defaulted into the default investment option)?



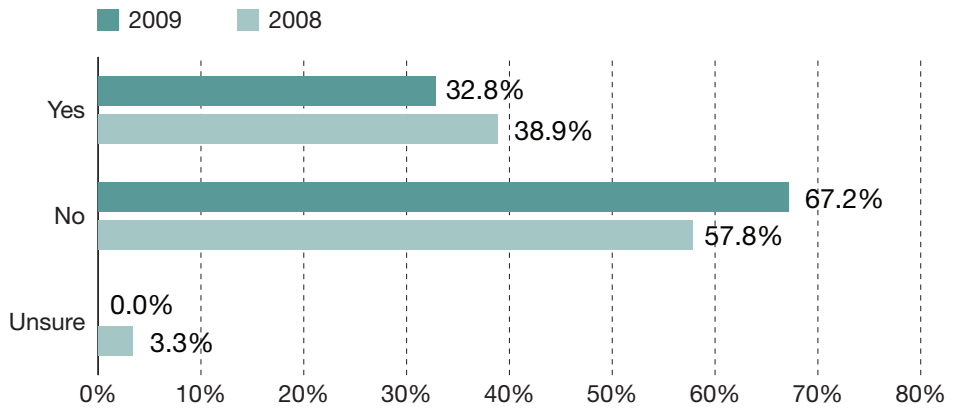
Why will there be no reenrollment?



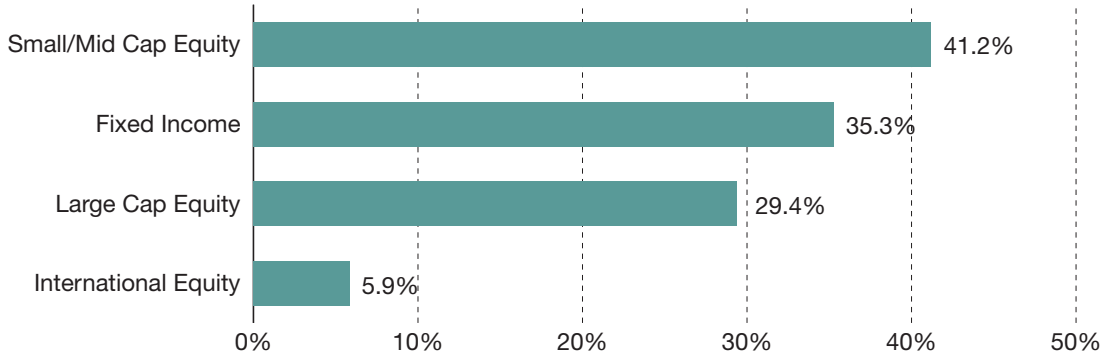
Manager/Fund Replacement

Despite the high prioritization of fund/manager due diligence going into 2009, there were fewer fund replacements due to performance-related reasons during the year (32.8%) than in 2008 (38.9%). Many plan sponsors have been uncertain as to how to proceed in the face of ongoing market and manager upheavals and have taken a wait-and-see approach as the markets and investment management industry settle. Small/mid cap equity (41.2%), fixed income (35.3%) and large cap equity (29.4%) asset classes were most frequently replaced in 2009.

Were fund managers/funds replaced in the past year due to performance-related reasons?



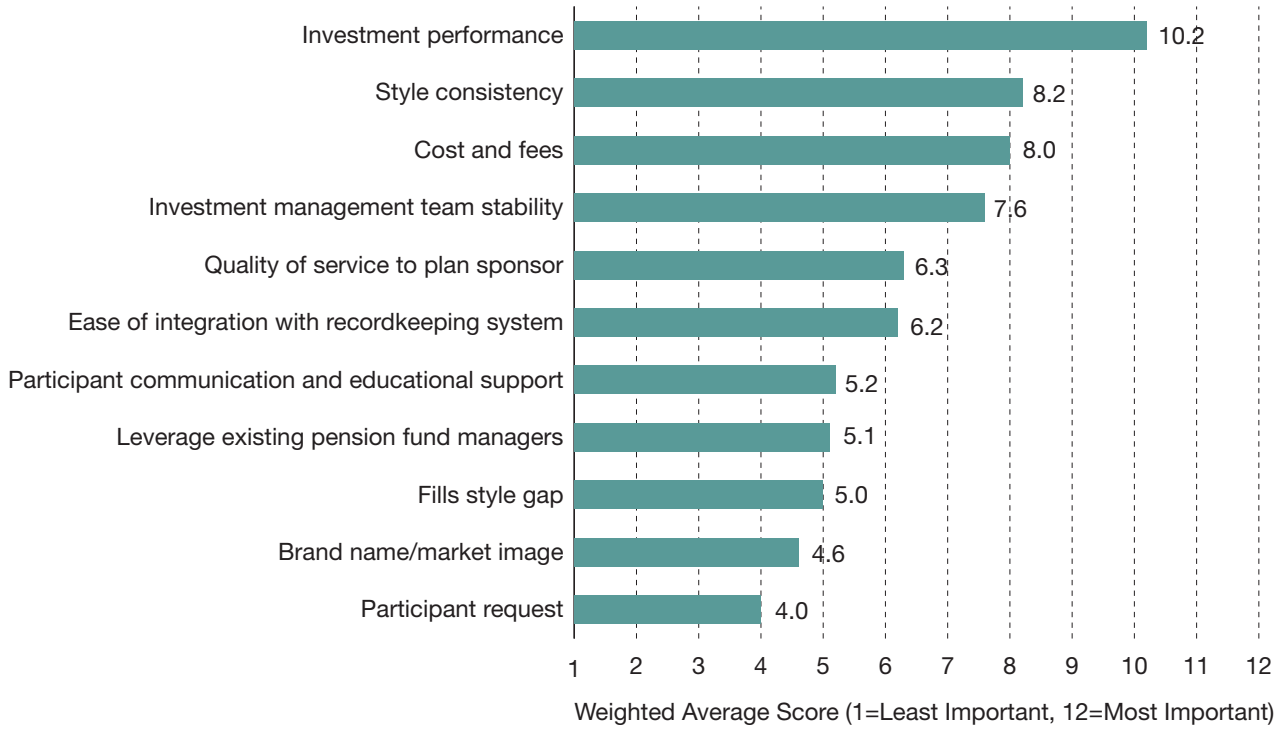
Of those making changes, funds replaced:



Investment Selection

As in past years, plan sponsors rank investment performance as the top key attribute in evaluating and selecting investment funds. However, style consistency moved up to the second spot in 2009 from fifth in 2008. This shift undoubtedly owes to the myriad of organizational changes (restructuring, layoffs and general consolidation) that occurred among investment managers in the wake of the market collapse. In addition, plan sponsors have little patience with changes in an investment approach that could lead to whipsawing as the market began to recover. Participant requests once again rank lowest on the scale of fund selection attributes.

What are the key attributes in the evaluation and selection of investment funds?



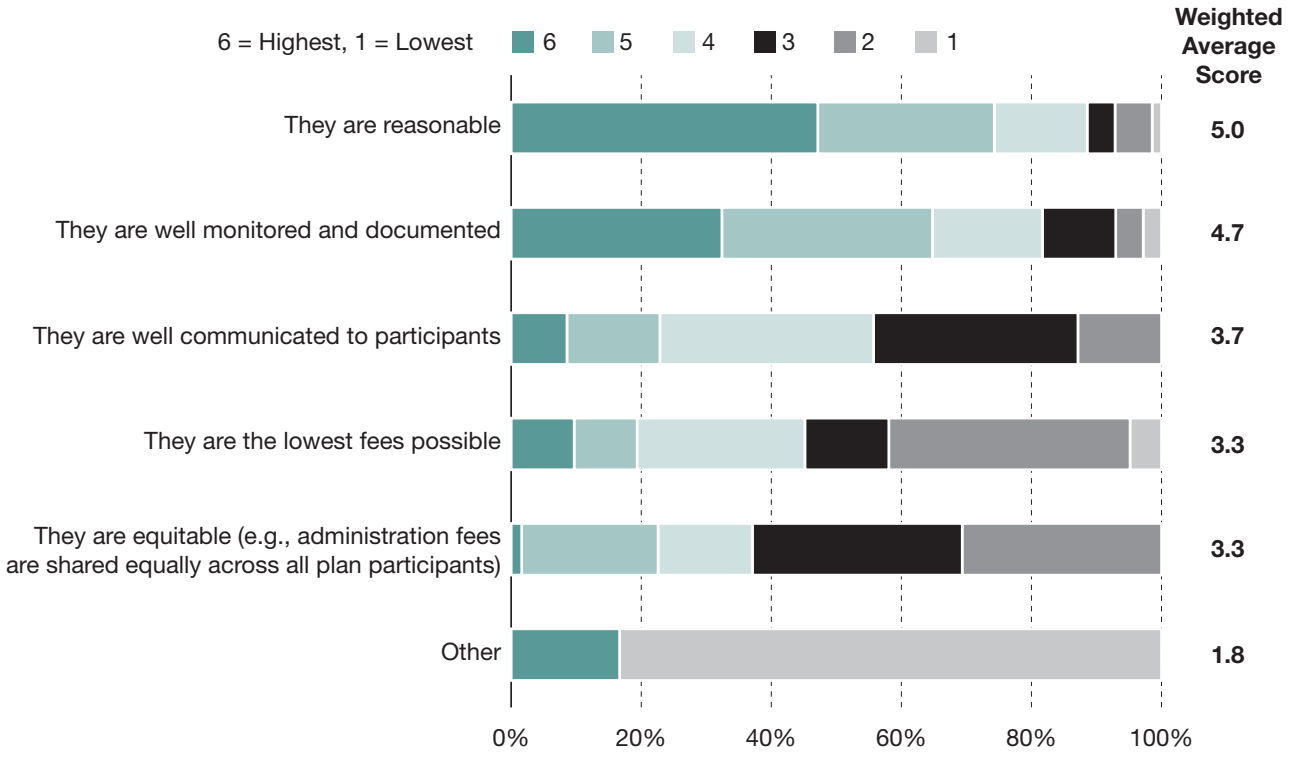
Fees: Areas of Focus in 2010

Plan sponsors' three main priorities in 2010 concerning DC plan fees:

1) They are reasonable,
2) well monitored and documented, and
3) communicated well to participants.

Interestingly, ensuring that fees are the lowest possible ranks the same in importance as ensuring that fees are equitably paid by participants in the plan. ERISA does not require that plan fees are the lowest possible, but rather that they are reasonable relative to the services provided. On the other hand, equitable fee payment may become increasingly important as regulators require greater fee disclosure by plan sponsors to DC participants.

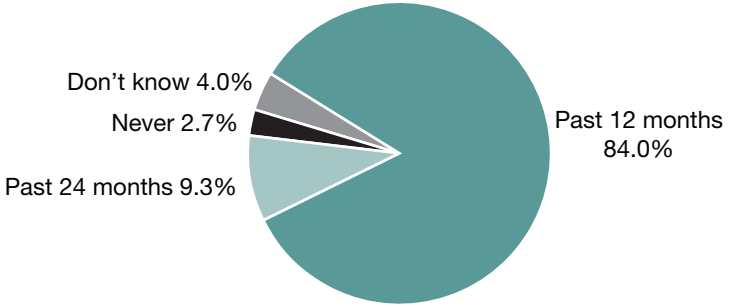
What are your key areas of focus around DC plan fees in 2010?



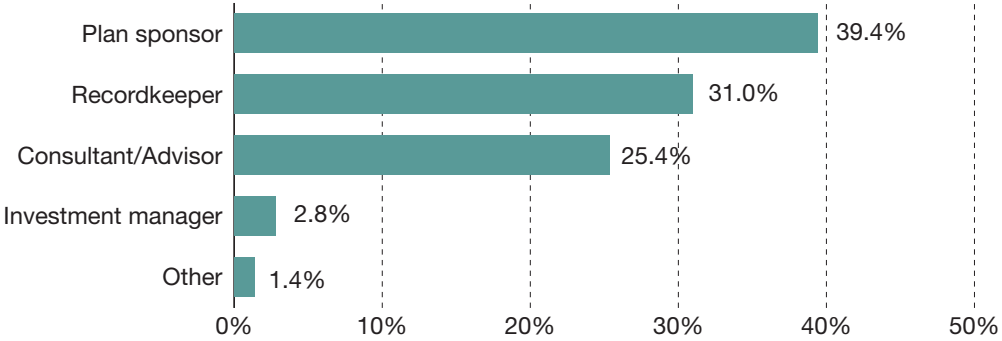
Fee Calculation

The focus on fees is underscored by the fact that virtually all of the plan sponsors in the survey sample (93.3%) have calculated their DC plan fees within the past 24 months. Most (84%) have done so within the past year. Nearly two-fifths (39.4%) of plan sponsors were responsible for the fee calculation, while the rest generally relied on a recordkeeper or consultant. Fewer plan sponsors found that fees were higher than expected in 2009 than in 2008 (7.1% versus 13.4%, respectively). This may be attributable to last year's market collapse, which eroded asset bases, dragging down asset-based fees and reducing costs in situations where such fees are used. Further, plan sponsors' ongoing scrutiny of fees can also be credited with assuring that fees are more inline with expectations.

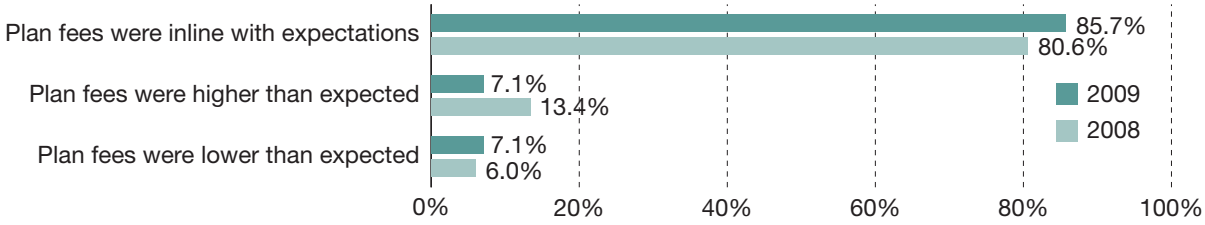
When was the last time you calculated fees for your DC plan?



Who was responsible for your fee calculation?



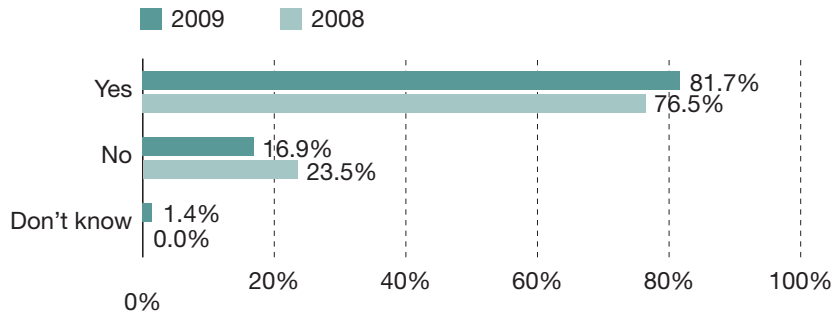
What was the outcome of your fee calculation?



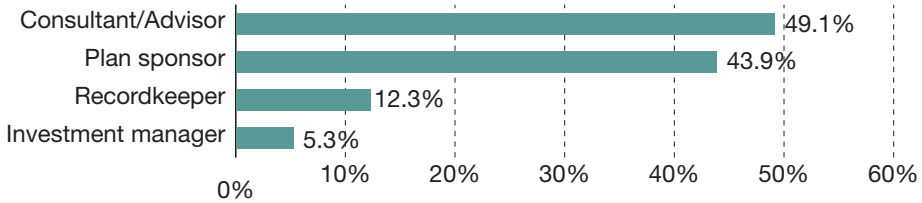
Fee Benchmarking

Most plan sponsors that calculated plan fees also benchmarked them (81.7%) in 2009, an increase from 2008 (76.5%). Benchmarking of plan fees is typically performed by the consultant/adviser (49.1%) followed by the plan sponsor (43.9%). Techniques vary broadly. The most common benchmarking tools are databases, such as the consultant's fee database (43.6%) or the recordkeeper's (29.1%). One-quarter (25.5%) of respondents use general fee benchmarking data sources, such as from the Committee on Investment of Employee Benefit Assets (CIEBA).

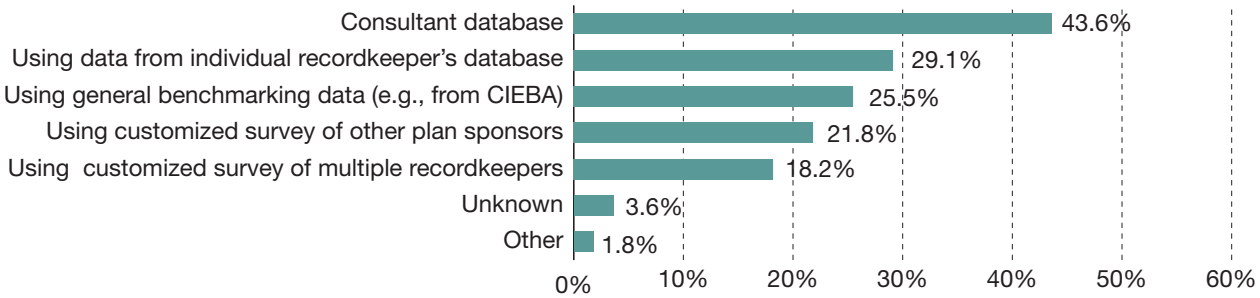
In calculating fees, did you benchmark the level of fees?



Who was responsible for the fee benchmarking?[A]



How was benchmarking accomplished?[A]



[A] Multiple responses were allowed.

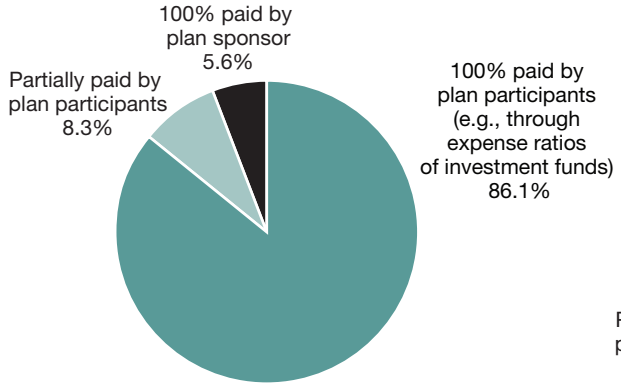
Payment of Fees

While most plans' investment management fees are entirely paid by participants (86.1%)—typically through the investment funds' expense ratio—less than half (43.2%) of plans' administrative fees are entirely participant paid. One-third (33.8%) cite a split payment by participants and the plan sponsor and one in five (21.6%) report that administration fees are entirely paid by the plan sponsor.

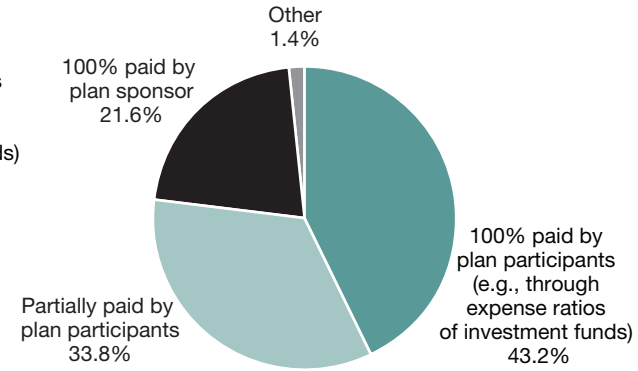
Participants pay administration fees primarily through revenue sharing (64.9%) followed by a percentage fee that is assessed across some or all funds outside of the investment management fees (29.8%). One-quarter (24.6%) use an explicit per-participant fee as a means of payment.[A] According to this year's survey, just 2.7% of plans with revenue sharing have such arrangements across all funds. Index and stable value funds do not commonly have revenue sharing arrangements. Among plans offering company stock, just over one-third (37.8%) apply an explicit fee (dollar or basis point) for administration. This is generally paid by the participant, most commonly as a basis-point fee (24.1%).

The issue of fairness may be raised when participants pay varying levels of administrative fees based on the funds they select (uneven revenue sharing across funds). This is likely to become an increasing area of focus if regulators require plan sponsors to reveal more detail about revenue-sharing arrangements to plan participants.

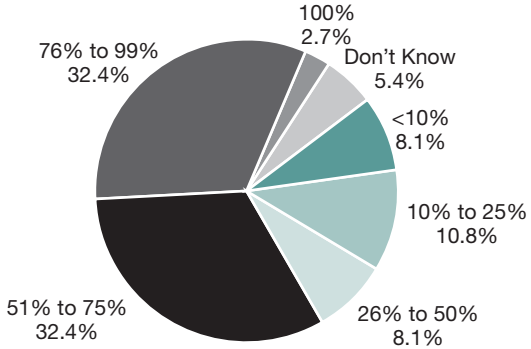
How are the plan's investment management fees paid?



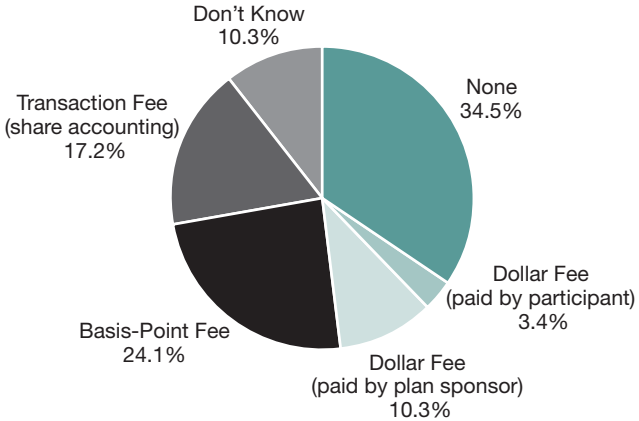
How are the plan's administrative fees paid?



What percentage of the funds in the plan offer revenue sharing or some kind of administrative allocation back from the investment fund?



What type of administrative fees are applied to company stock?



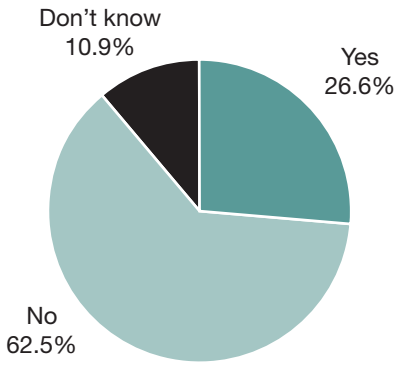
[A] Multiple responses were allowed.

ERISA Accounts

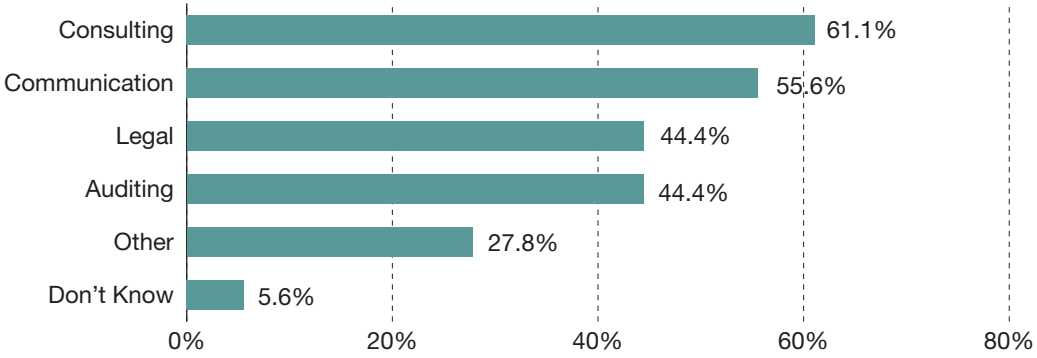
Some plans with revenue sharing find that the funds within their investment menu generate excess revenue relative to the amount required to pay plan administration fees. One way to address this situation is to create an ERISA account (also known as a plan reimbursement account), which is typically held outside of the plan by the recordkeeper. Excess revenue sharing flows to the account and is used to cover plan-related expenses.

In 2009, 26.6% of plan sponsors used an ERISA account. Consulting is the most common expense paid through the ERISA account, followed by communication, legal and auditing. Interestingly, about one in 10 plan sponsors are unsure whether or not they have an ERISA account.

Do you currently have an ERISA-type account?



What expenses are paid through the ERISA-type account?[A]

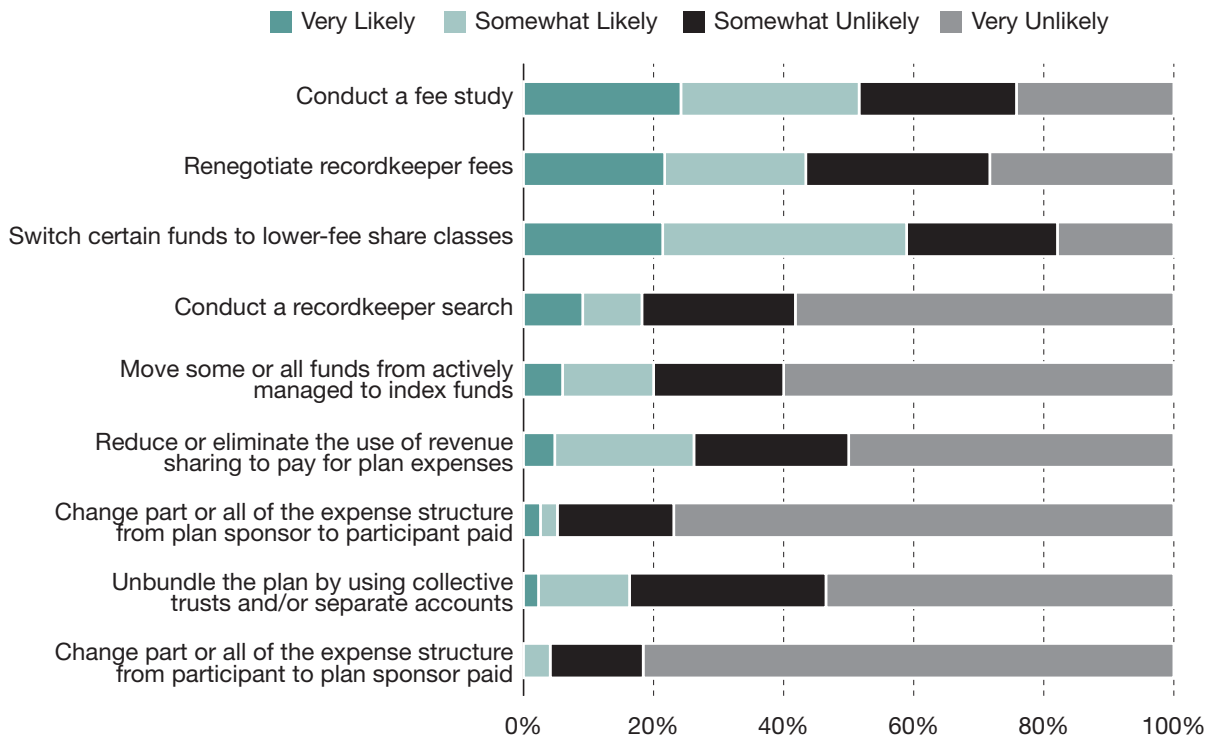


[A] Multiple responses were allowed.

Fee Activities in 2010

In 2010, plan sponsors are most likely to conduct a fee study or switch certain funds to lower-fee share classes, but are least likely to change their expense structure (e.g., from participant paid to plan sponsor paid or vice versa). More than one in four plan sponsors (26.2%) express some interest in reducing or eliminating the use of revenue sharing to pay for plan expenses. Often this goal is tied to a desire to achieve more equitable fee payment across plan participants. Although, as observed earlier, equitable fee payment is not a key area of DC plan sponsor focus.

What steps around fees are you most likely to engage in for 2010?

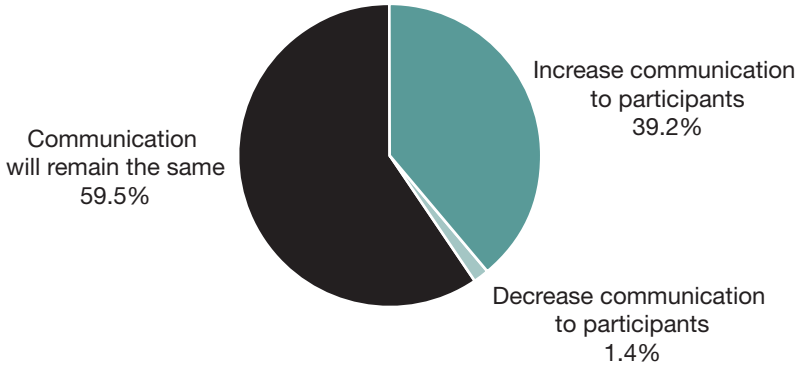


Participant Communication

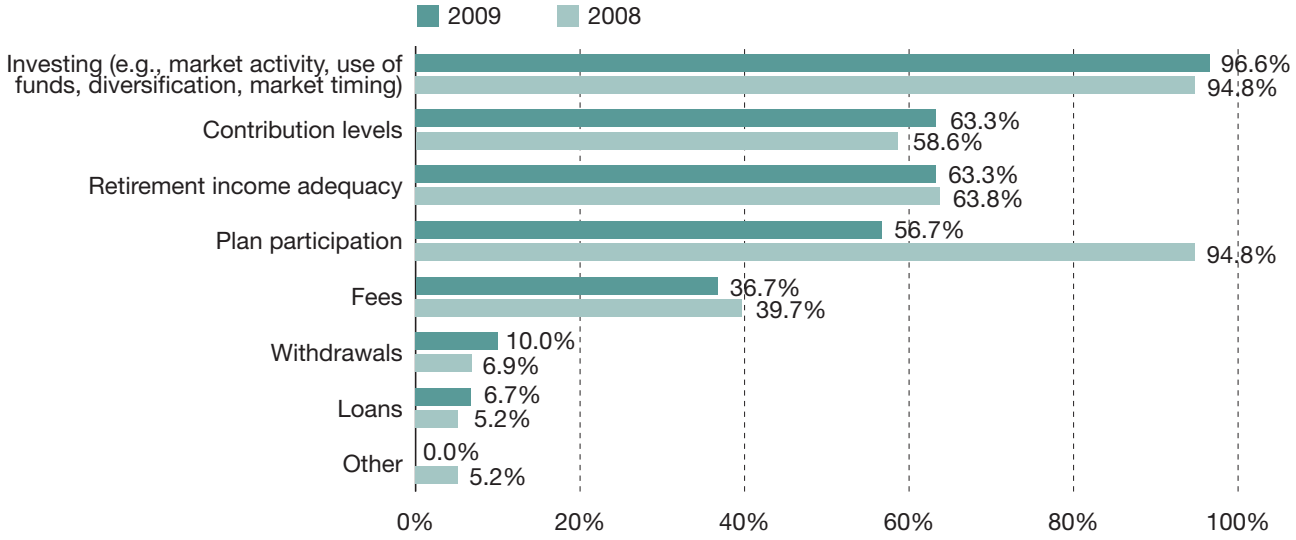
Most plan sponsors (or their recordkeepers) engaged in special communication to participants this year (90.7%). Over one-third (37.8%) involved communication or education about plan fees. Another area of communication focus cited in both 2008 and 2009 is investing.

For 2010, about two-fifths (39.2%) of respondents will increase communication to participants. Investment topics, such as market activity, use of funds, diversification, market timing, and target date communication, will continue to be a primary focus (96.6%). Communication around plan participation in 2010 will be overshadowed by communication around retirement income adequacy and contribution levels (63.3% each). Increased communications around contribution levels relative to 2008 are likely due to concerns about participant deferral rates in light of tougher economic times and the fallout from the elimination of company contributions, as participant deferral rates tend to decline when company matching contributions are eliminated.

What actions around plan communication/education are you likely to engage in for 2010?



What will the areas of increased communication 2010 be?[A]



[A] Multiple responses were allowed.

Author Biographies

Lori Lucas, CFA, is an Executive Vice President and Defined Contribution Practice Leader. Lori is responsible for setting the direction of Callan's DC business, providing DC support both internally to Callan's consultants and externally to Callan's clients, and developing research and insights into DC trends for the benefit of clients and the industry. Lori is a member of Callan's Management Committee, and is a shareholder of the firm.

Formerly, Lori was Director of Retirement Research at Hewitt Associates. Lori has also served as a vice president at Ibbotson Associates, a pension fund consultant at J.H. Ellwood & Associates, and an analyst and product development leader at Morningstar, Inc.

Lori received a Bachelor of Arts from Indiana University and earned a Masters from the University of Illinois. Additionally, she earned the right to use the Chartered Financial Analyst® designation. Lori's views have been featured in The Wall Street Journal, The Chicago Tribune, Pensions & Investments, Plan Sponsor Magazine, The Washington Post, USA Today, Bloomberg, CNN, CFO-TV, The New York Times, Newsweek, Money Magazine, the Baltimore Sun, The Boston Globe, and WGN, among others. Lori's writings have been published in Benefits Quarterly and the Pension Investment Handbook, among others. Lori is a columnist for Workforce Management online magazine, and she is Executive Vice Chair of the Employee Benefit Research Institute's Retirement Research Committee. Lori is also a frequent speaker at pension industry conferences.

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Prior to joining Callan Associates, Jimmy served over two years as a United States Peace Corps Volunteer in the Kingdom of Tonga. He served as project manager for the Future Farmers of Tonga program and taught at Queen Salote College.

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Callan Associates would like to express our appreciation to the participants who took the time and effort to provide us with this valuable information.

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