

FOR IMMEDIATE RELEASE  
September 2, 2008

CONTACT: Mr. Joshua Dietch  
Managing Director  
Chatham Partners  
(781)314-0610  
jdietch@chathampartners.net

**WALTHAM, MA**, September 2, 2008 – PPA and the creation of the long-term Qualified Default Investment Alternative (QDIA) has brought about a degree of change in the defined contribution (DC) marketplace that has not been seen since the introduction of daily valuation recordkeeping systems to mutual funds. Newly created plan design safe harbors such as auto-enrollment and new features such as auto-escalation coupled with the QDIA have the potential to radically change not only how employees are enrolled in retirement plans but also how they contribute and invest for their personal retirement savings needs.

To assess how plan sponsors and their intermediaries are evaluating and making QDIA elections, Chatham Partners recently completed a research study, entitled, "*And They're Off! – The Race to Gather QDIA Assets - An Assessment of Selection and Evaluation Criteria of QDIA Options by Plan Sponsors and Their Intermediaries*". Not surprisingly, there is a rush to capture QDIA assets. For those seeking to manage these assets, traditional means of gaining market share may no longer apply. Thus, it is critical for investment managers and recordkeepers to fully understand the decisions plan sponsors are making regarding the QDIA for their DC programs, how those decisions are made, what factors influence those decisions, and what role they can play in the decision making process.

Chatham's research reveals that 66% of plan sponsors have already chosen a QDIA provider, making the struggle to win over the remaining 34% of undecided sponsors all the more important. Though recordkeepers with investment management affiliates appear to be best positioned to capture QDIA assets, this study suggests that there are multiple opportunities for investment managers, recordkeepers, and intermediaries to differentiate themselves through either the products or services they provide.

"What struck us as surprising is the sheer rapidity at which plan sponsors have made an initial QDIA election. Clearly plan sponsors have seized upon the "safe harbor" provided by the DoL giving a clear advantage to managers' existing QDIA-eligible products in the marketplace. Further, our research also suggests that plan sponsors were looking for a better way for their participants to be engaged in saving for retirement, and the response to PPA in general and the QDIA regulations in particular largely validates that," noted Joshua Dietch, Managing Director at Chatham Partners.

**Additional key findings from the research include:**

#### *Attitudes of Plan Sponsors*

- Two-thirds of plan sponsors have selected a QDIA despite limited understanding of QDIA regulations and alternatives. Among plan sponsors that have selected a QDIA, target date funds are the most frequently cited option followed by risk-based / balanced funds, and managed accounts. However, plan sponsors who have not selected a long-term QDIA do not demonstrate a strong preference for one alternative compared to another. In fact, almost 40% express uncertainty as to which option they will ultimately choose, suggesting that opportunities remain to convince them of the merits of target date, risk-based / balanced, or managed account approaches.
- The manner in which plan sponsors have historically evaluated target date or risk-based / balanced funds is consistent with the risk managed nature of these products. Accordingly, plan sponsors commonly cite pricing / fees, performance related attributes, fund diversification, and risk / return characteristics as some of the more important attributes they took into consideration when selecting a fund.
- Overall 19% of plan sponsors indicate that they use an index manager to manage their QDIA. However, almost two-thirds of plans that chose index managers had plans of at least \$250 MM in assets. Sponsors that chose index managers primarily did so because the products are low cost, avoid security selection and market risk, and are easy to explain to plan participants.
- Large plan sponsors are more likely to want to customize their QDIA fund to meet plan specific criteria or objectives. Common rationale for customization include tailoring the risk profile to be reflective of employee risk tolerance and demographics, a desire to actively play a role in underlying manager selection, and minimizing fiduciary risk.

### *Role of Intermediaries and Recordkeepers*

- 86% of plan sponsors indicate that they are reliant upon some form of intermediary to assist them with the general management of their DC plan investments, and 79% indicate they used or intend to use an intermediary to assist in the selection of their plans' QDIAs. The opportunity created by QDIAs is also driving change for intermediaries. It has forced them to devote resources to analyzing new products and developing services to meet the evolving needs of plan fiduciaries. Specifically, intermediaries are focusing their efforts on improving how plan sponsors implement QDIA options and the evaluation and monitoring services they typically provide.
- Recordkeepers play an important role in QDIA selection. Plan sponsors indicate that their recordkeeper either offered a proprietary option managed by an affiliate of the recordkeeper or offered a range of options including one managed by an affiliate 89% of the time. However, on average the recordkeeper is making a specific QDIA recommendation almost half of the time. This dynamic is generally consistent across asset segments save for the very largest plans that often draw a distinction between how they evaluate and purchase recordkeeping and plan investments.

### *Future Implications*

- The perceived magnitude of the QDIA opportunity is enticing investment consultants into the investment management arena. Many firms state that they are at least considering developing QDIA manufacturing capabilities. Most consider creating target date or risk-based / balanced funds as a logical extension of the manager and investment research they presently provide to plan sponsors. While many investment managers point to the potential conflict of interest in consultants attempting to make the transition to money management, plan sponsors who would appear to at least give consideration to the idea seem less concerned.
- The opportunity to be a long-term QDIA manager is "winner take all". Investment managers seeking to gain a foothold in this product category will likely need to unseat an incumbent to gain market share, as the majority of respondents who have selected a QDIA are very satisfied with their QDIA manager. Of the respondents who expressed dissatisfaction with their QDIA manager, only one-third are at least considering changing their QDIA manager. Interestingly, the largest plans (>\$1 BN), in addition to being the most likely to have selected a QDIA option, seem to be the most content with their QDIA manager.

The practical implication of this research is that there are multiple opportunities for investment managers to differentiate themselves in the race to gain QDIA assets. Some will choose to do so by providing comprehensive solutions that integrate plan administration, participant servicing, and plan investments. Others will plumb the niches to find pockets of plan sponsors that perhaps desire a specific skill set or a unique product capability. However, a common denominator is that the winners will define themselves by focusing not only on introducing new processes and products but also on the results generated for plan sponsors on behalf of their participants. Thus, once the euphoria of PPA and QDIA has subsided, the real winners will be intermediaries, recordkeepers, and investment managers who have aligned themselves with this new paradigm of DC plan management.

---

The 103 page report's foundation is in-depth online surveys completed by 499 plan sponsors affiliated with corporate defined contribution plans ranging in size from \$1 MM in assets to more than \$1 BN in assets and interviews with 60 investment consultants and financial advisors. For more information about Chatham Partners please visit [www.chathamllc.com](http://www.chathamllc.com) or call (781)314-0600. For more information about this research study, please contact Joshua Dietch at [jdietch@chathampartners.net](mailto:jdietch@chathampartners.net) or call (781)314-0610.

Chatham Partners, based in Waltham, Massachusetts, provides strategic advisory services and market research to the financial services industry.