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New Research from EBRI:

Target-Date Funds: Participants Are Younger, Have Lower Account Balances, Shorter Tenure—But Stick With the Funds

WASHINGTON—The use of target-date funds, a relatively new 401(k) plan option, is more likely among participants who are younger, have lower account balances, and have shorter tenure at their current job, according to a study released today by the nonpartisan Employee Benefit Research Institute (EBRI). The reason for this pattern is that new workers are the most likely to be automatically enrolled in their employer's 401(k) plan, with a target-date fund (TDF) often being the default option, says the study in the July 2010 *EBRI Notes*, available at www.ebri.org

The EBRI analysis also shows that target-date users are likely to stick with their fund over time.

Target-date funds are designed to make it easier for Americans to save for retirement by providing simplicity for investors. The name of these funds usually includes a date that represents the year in which the investor intends to retire. While their growth has been rapid in 401(k) plans in recent years, TDFs are still relatively new for most participants.

As a result, not much research has been done on how participants use these funds over time. The study focuses on 401(k) participants who were in plans that offered TDFs in 2007 to see whether they remained in TDFs, moved out of TDFs, or moved into TDFs if they were not already using them. The study uses the data in the EBRI/ICI Participant-Directed Retirement Plan Data Collection Project, which in 2007 had 21.8 million participants from 56,232 plans across a spectrum of plan administrators.

The share of all 401(k) plan participants using TDFs increased from 25 percent in 2007 to 31 percent in 2008, the study reports. Future growth can be expected as the participants in TDFs remain in them and as new participants sign up for them voluntarily or through an automatic enrollment default option. Therefore, the study says, the design of TDFs (especially the investment allocation “glide path”), as well as participants’ understanding of these funds, will become more critical to the future success of 401(k) plans.

Here are some of the other key points in the study:

- Of those participants having an allocation to TDFs in 2007, 93.9 percent still had some of their account balance allocated to TDFs in 2008. Nearly 10 percent of participants who were in a plan in 2007 that offered TDFs but did not use them in 2007 were using them in 2008.
- Of those participants who were in a plan that offered a TDF in 2007 and were still in the EBRI/ICI database in 2008, 36.0 percent had at least some of their account balance in TDFs. By 2008, of this same group of participants, 39.8 percent had at least some of their account balance in TDFs.
- Participants with the lowest salaries were more likely to stay in TDFs and begin using them in 2008. However, as salaries increased, there was no significant difference in new TDF use.
- As a participant’s plan size increased, the likelihood of new TDF use in 2008 increased, but the probability of continuing use showed very little change across plan sizes. In plans with 1–10

participants, 94.8 percent of those using TDFs in 2007 still had dollars allocated to them in 2008, compared with 93.0 percent of those in plans with more than 10,000 participants.

- The participants most likely to *stop* using TDFs and least likely to *start* using them if they have not already done so are those with the highest levels of tenure and the highest account balances. Of those participants in 2007 with 30 or more years of tenure and having some of their account balance allocated to TDFs, 85.8 percent continued to have some assets in TDFs in 2008. For comparison, of participants in 2007 with two to five years of tenure, 95.5 percent remained allocated to TDFs in 2008 after having done so in 2007.
- The average age of those participants using TDFs in 2007 was 43.1 and in 2008 it was 42.4, compared with 45.6 and 46.2, respectively, for those participants not using TDFs. The average age for those using TDFs in both years was 42.9.

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