Default Investment Strategies
for
Defined Contribution Plans

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Summary

As defined contribution plans have progressed to automatic enrollment and allow participant investment direction, the need for an effective default investment strategy has become more acute. In the U.S., this has been codified in the Pension Protection Act of 2006 and the subject of final regulations issued by the U.S. Department of Labor.

Plan fiduciaries have considered several alternatives in developing their respective default investment strategies. The most popular alternatives have been target date funds, lifecycle funds, balanced funds, managed accounts sponsored by banks and insurance companies and in-house managed funds.

Target date funds have been the most popular in the U.S., but have created some confusion among investing plan participants and plan fiduciaries. Performance by many target date funds since the economic crisis of 2008-09 has been disappointing and caused many plan fiduciaries to reconsider their default investment strategies. Both the U.S. Department of Labor and Securities Exchange Commission have since proposed rules requiring greater disclosure by target date funds.

Critics of target date funds have cited the conflicts-of-interest created by the fund-of-funds structure of most target date funds and potentially excessive fees created thereby. This has created a new landscape for plan fiduciaries in developing their default investment strategies.