Case Study

Implementing a Complete Target-Date Fund Solution

J.P. Morgan
As clients face fundamental changes in the way they do business – driven by regulation, fiduciary obligations, disappointing investment returns and increasing correlations – they seek a partner that can provide effective solutions in a risk-controlled environment. Our client needed an investment solution that offered flexibility and control, and employed a leading technology infrastructure that allowed them to implement a custom target-date fund structure into their retirement plan in a cost-efficient and flexible manner.

The Client

A leading global financial services firm approached J.P. Morgan looking to improve their defined contribution, or 401(k), offering. The client has both a large and mature defined benefit plan and a new, rapidly growing defined contribution plan. The client had an aggressive agenda – their investment committee required the ability to continuously assess current plan options and seek new options that would benefit plan participants. Additionally, they sought to add an auto-enrollment feature and default investment options, as well as simplify their portfolio lineup. As such, the client was looking to offer target-date funds to their defined contribution offering.

The Need

A pension plan sponsor bears a fiduciary responsibility to ensure participant needs are fairly represented and appropriately addressed. There has been significant litigation over the past five years where firms have been held liable for failing to act in the best interests of plan participants. While specifics differ, many of these suits have claimed that plan options were not cost-effective, participants were misled about the nature of their investments, and that adequate investment strategies were not offered.

J.P. Morgan’s client received feedback from its plan participants that the investment decision-making process was difficult and overwhelming, and despite a variety of educational tools, employees still struggled to make adequate investment and asset allocation choices. Additionally, the client observed that many of its employees were taking no action to save for their retirement, therefore putting themselves in a more challenging financial situation. To address this concern, the plan’s investment committee sought to implement an auto-enrollment feature obligating new employees to participate in retirement planning even if they took no overt actions.

Federal regulation mandates what type of investment options may be used in auto-enrollment activities, specifically The Pension Protection Act of 2006, which requires use of a “Qualified Default Investment Alternative,” or QDIA. Target-date funds, among other options, were highlighted as acceptable QDIAs.

To represent the best interests of their plan participants, the client had four main investment priorities: 1) diversification and access to new asset classes, 2) open architecture 3) cost efficiency, and 4) a comprehensive solution for ease of implementation and administration.

Diversification and Access to New Asset Classes

The client’s investment committee wanted to offer their participants access to extended and alternative investment options. There has been increasing, broad-based interest in investment strategies that offer a diversifying effect, including investing in real assets (commodities, real estate, timber, etc.). Furthermore, alternative style portfolios that employ shorting and derivatives strategies have been gaining more mainstream acceptance in the pension market and may generate investment returns less correlated with the broader markets. For certain asset classes, passive or index funds can also be appropriate investment choices. The client wished to be able to offer the best options as they continue to arise in the marketplace.

Open Architecture

The client saw an open architecture framework as vital to representing the best interests of their plan participants. This would allow the client to change underlying managers.
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by removing underperformers and adding new options as necessary in a simple manner. Open architecture should facilitate these modifications in a virtually seamless manner with minimal costs.

COST EFFICIENCY

J.P. Morgan's client sought a customized, yet cost-effective solution, and some custom target-date funds can offer such benefits. For example, custom target-date funds may utilize collective trusts instead of, or in addition to, mutual funds. Collective trusts tend to have fewer costs associated with their maintenance and are therefore generally less expensive than mutual funds. Additionally, for certain asset classes, the client determined that passive investment approaches offered the best cost/benefit tradeoff, thus the need to offer both passive and active investments was important.

While the existing defined contribution plan offered participants a broad array of investment options at appropriate pricing levels, creating a target-date fund series would allow participants investment exposure to these assets and strategies in the context of a single, diversified portfolio.

COMPREHENSIVE SOLUTION

Offering a target-date fund requires coordination across a number of different parties, including investment managers, record keepers, glide path managers, and back office administration providers. An end-to-end, comprehensive solution at a reasonable price point was most desirable.

The Solution

The client selected J.P. Morgan Asset Management and Investor Services, using J.P. Morgan Cash Allocation and Rebalancing Solution (CARS™), to manage and service their new target-date fund offering. The deciding factors included the firm's offering of an integrated end-to-end, bundled target-date fund solution at a compelling price, innovative investment strategies, and the ability to support this complex, customized open architecture.

J.P. Morgan CARS™ Cash Allocation and Rebalancing Solution

CARS delivers highly flexible, controlled and scalable support of complex fund structures such as target-date funds. It enables plan sponsors to create and deliver innovative fund of fund structures, particularly custom, open-architecture target-date funds, with flexibility, efficiency and control. CARS supports custom target-date funds by enabling clients to implement a unique glide path with any configuration of underlying fund types. Furthermore, CARS is integrated with J.P. Morgan’s custody and accounting systems.

Why J.P. Morgan

Financial stability is a key component in maintaining J.P. Morgan’s competitiveness and one of the key factors behind our commitment to pension plans. To support clients’ end-to-end requirements, J.P. Morgan builds on its financial strength and global capabilities, to integrate and streamline services. And, for our clients this affords security and assurance in areas fundamental to their business.

J.P. Morgan is strategically and operationally committed to providing the full array of services for defined contribution plans, ranging from ‘line item’ accounting for mutual and collective trust funds that are part of the plan, through the daily valuation and unitization of separately managed accounts, and the calculation and delivery of NAVs to the plan’s pension administrator. J.P. Morgan supports complex unitized fund of fund investment structures – including master trusts shared by defined benefit and defined contribution plans – in support of the creation of highly efficient and proprietary investment options for defined contribution plans. J.P. Morgan CARS is an innovative and competitively differentiating solution that enables clients to create and securely deliver highly efficient investment options to their defined contribution plan participants, including custom/open architecture managed allocation funds, such as balanced, target risk and target-date funds.