STRATEGIES FOR SUCCESS

WINTER 2019

Engaging fiduciary support

As plan sponsors know, running a retirement plan well is not an easy undertaking. There are many moving parts — administration, investment management, recordkeeping, communication — all involving detailed requirements and numerous interrelated activities.

Complexity aside, plan sponsorship also exposes employers to significant risk in their role as plan fiduciaries. Various lawsuits targeting plan sponsors have raised awareness of what proper fiduciary oversight of a plan looks like and the penalties that can be assessed for fiduciary breaches.

Increased awareness of fiduciary responsibilities has fueled employer interest in fiduciary support solutions. Before making any decision, however, employers will want to fully understand the levels of fiduciary support that are available — and the significant differences among them.

Fiduciary duties — an overview

Function, rather than title, generally determines a person's fiduciary status under federal pension law (ERISA). A person is a fiduciary to the extent that the person:

- Exercises discretionary authority or discretionary control over the management of a plan or exercises authority or control over the management or disposition of the plan's assets;
- Provides investment advice to the plan for a fee or other compensation (or has the authority to provide plan investment advice); or
- Has discretionary authority or discretionary responsibility over plan administration.

Every plan must have one or more "named fiduciaries" who are responsible for the plan's overall operation and administration. A plan may have procedures for allocating fiduciary duties among several named fiduciaries. Additionally, a plan may allow a named fiduciary to designate someone who is not a named fiduciary to carry out certain fiduciary duties. However, trustee responsibility may not be delegated to a person who isn't a named fiduciary.

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5 KEY PRINCIPLES THAT DRIVE RETIREMENT PLAN SUCCESS

EFFECTIVE PLAN DESIGN AND ADMINISTRATION

Help meet the organization's goals while also encouraging and enabling employees to pursue their retirement goals.

MEET FIDUCIARY RESPONSIBILITIES

Operate the plan in compliance with a strict set of fiduciary and regulatory standards.

COST AND RESOURCE MANAGEMENT

Save time, effort, and money by implementing the right solutions and working with the right team.

OPTIMIZE INVESTMENTS

Offer an investment menu that is diversified to meet employees' varying time horizons and goals.

RETIREMENT READINESS

Give plan participants access to guidance, advice, and tools to measure and monitor their progress toward achieving their retirement goals.

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Plan fiduciaries have considerable responsibility. They must:

- Follow the plan documents (unless the documents are inconsistent with ERISA);
- Act solely in the interests of the plan participants and their beneficiaries and for the exclusive purpose of providing benefits to them;
- Act with the care, skill, prudence, and diligence that a prudent person would exercise under similar circumstances;
- Ensure that the plan's investments are diversified (unless it is clearly prudent not to do so under the circumstances); and
- Pay only reasonable plan expenses.

Plan fiduciaries are considered "parties in interest" to the plan and, as such, are not allowed to engage in certain transactions with the plan. Examples of prohibited transactions include:

- Selling, exchanging, or leasing property;
- Lending money or extending credit; and
- Furnishing goods, services, or facilities.

Fiduciaries are also prohibited from self-dealing. Various restrictions prevent a fiduciary from deriving personal gain from actions that involve the plan.

Fiduciaries who breach their responsibilities may be personally liable to restore the plan to the condition it was in prior to the breach, including restoring any monetary losses and returning any profits made through the improper use of plan assets. Violations of the prohibited transaction rules can also result in the imposition of excise taxes.

Engaging providers for fiduciary support

Many employers seek assistance from professionals when it comes to the selection and management of plan investments. There are three levels of fiduciary support:

3(21) investment advisor. An investment advisor under Section 3(21) of ERISA provides investment recommendations with respect to a plan's investment menu but usually does not have discretionary authority over the plan's assets. The fiduciary liability for investment decisions rests with the plan's trustee. The table below lists the specific functions that a 3(21) investment advisor may perform.

3(38) investment manager. Instead of providing investment advice only, an ERISA Section 3(38) investment manager generally has the discretion to make investment decisions for the plan. In this capacity, the investment manager would typically determine the plan's investment menu, monitor the investments, and replace them as needed. Additional services may include making premixed model portfolios or managed accounts available to plan participants. The specific fiduciary responsibilities assumed by the investment manager are described in a written service agreement. The fiduciary who appoints the investment manager remains responsible for monitoring the investment manager's performance.

Discretionary trustee. As a "named fiduciary" in the plan document, a discretionary trustee assumes full control and authority for managing the assets of the plan. Hiring a discretionary trustee relieves the plan sponsor of most of the day-to-day oversight of the plan and affords the broadest level of fiduciary protection for the plan sponsor. However, the plan sponsor still retains responsibility for monitoring the trustee.

In addition to the above fiduciary support models, there are various administrative outsourcing arrangements. While many administrative functions are not fiduciary in nature, fiduciary administrative services might include responsibilities such as approving participant loans and distributions or authorizing other plan transactions.

Talk to us

If you are considering hiring one or more professional providers to serve your plan in a fiduciary capacity, make sure you understand the different models that are available in the marketplace. Your SunTrust representative can help you weigh the options and select the model that is right for you. And, be sure to ask about our Fiduciary Fitness training program for plan sponsors.

3(21) INVESTMENT ADVISORY VS. 3(38) INVESTMENT MANAGER VS. DISCRETIONARY TRUSTEE

Function	3(21) Investment Advisor	3(38) Investment Manager	Discretionary Trustee
Responsible for selection, monitoring, and replacement of plan investments	In conjunction with committee	√	√
Supplies and follows IPS	√	√	√
Named fiduciary in plan document	Must be in separate agreement	Must be in separate agreement	√
Naturally responsible for Section 404(c) compliance			√
Follow process designed to prevent prohibited transactions			√
Construct model portfolios which may be used as QDIAs	√	√	√
Custody of plan assets			√
Adhering to mandatory third-party audit requirements			√
Familiarity with ERISA standard of care	√	√	√

OPTIMIZE INVESTMENTS

A profile of 401(k) investors

401(k) plans are a primary retirement savings vehicle for some 55 million American workers of all ages. How much are they saving in their 401(k) accounts, and how are they investing their savings? Ongoing research from the Employee Benefit Research Institute (EBRI) and the Investment Company Institute (ICI) provides some interesting insights.[1]

Plan account balances

As of the end of 2016, the EBRI/ICI database included statistical information about 110,794 401(k) plans of various sizes and 27.1 million plan participants. Thirty-eight percent of the participants were in their twenties and thirties, 25% in their forties, another 25% in their fifties, and 11% in their sixties.

Across all 27.1 million participants, the average account balance was $75,358 and the median account balance was $16,836 at the end of 2016. This table shows the percentage of participants with account balances in different dollar ranges:

Size of Balance	% of Participants
< $10,000	41.0%
$10,000 - $50,000	28.4%
> $50,000 - $100,000	11.1%
> $100,000 - $200,000	9.0%
> $200,000	10.5%

In each age group, the average plan account balance tended to increase with more time on the job. For example, among participants in their forties, the average account balance was $166,953 with more than 20 years of job tenure; it was only $19,913 with up to two years of tenure.

Investment of plan assets

At the end of 2016, 67% of plan assets were concentrated in equity securities, including equity funds, the equity portion of target date and other balanced funds, and company stock. This table shows the average allocation of 401(k) plan accounts:

Investment Type	% of Account Balances
Equity funds	43.5%
Target date funds	21.3%
Non-target date balanced funds	6.1%
Bond funds	8.2%
Money funds	3.1%
Guaranteed investment contracts; other stable value funds	5.8%
Company stock	5.9%
Other	5.1%
Unknown	0.9%

The percentages do not add up to 100% due to rounding.

Forty-eight percent of participants had more than 80% of their plan accounts invested in equities. Only 7.6% of participants held no equities in their accounts.

Participants' asset allocations varied considerably depending on age. For example, participants in their sixties had an average of about 63% of assets in equity and balanced funds (including target date funds), compared to 84% of participants in their twenties.

Target date funds have become more popular and may serve as the default investment for a plan. The portfolio of a target date fund is typically rebalanced to become less focused on growth and more focused on income as the fund's target date approaches and passes.

At the end of 2016, 21.3% of 401(k) assets in the database were invested in target date funds. Younger participants had higher allocations to these funds. At year-end, 47.6% of the 401(k) assets of participants in their twenties were invested in target date funds. About 59% of recently hired participants – those with two or fewer years of tenure – held target date funds, compared to about 31% of participants with more than 30 years of tenure.

[1] "401(k) Plan Asset Allocation, Account Balances, and Loan Activity in 2016," ICI Research Perspective, September 2018

EFFECTIVE PLAN DESIGN AND ADMINISTRATION

Exceptions to the 10% Tax on Early Distributions

To encourage employees to participate in retirement plans, the federal tax law provides various tax-related benefits to plan participants. For example, contributions to a qualified retirement plan may be made pretax, which helps to reduce the current income taxes participants owe on their pay. Additionally, participants do not have to pay current taxes on any investment income that contributions earn. Income taxes on contributions and earnings are deferred until money is distributed to the participant from the plan. However, if a participant takes a plan distribution before reaching age 59½, the participant may have to pay a 10% penalty tax on the distribution in addition to regular income taxes.

There are circumstances when the 10% additional tax will not apply. Plan sponsors should familiarize themselves with these exceptions. These circumstances include distributions that are:

- Made to a beneficiary (or to the estate of the participant) on or after the death of the participant;
- Made because the participant has a qualifying disability;
- Made as part of a series of substantially equal periodic payments beginning after separation from service and made at least annually for the life or life expectancy of the participant or the joint lives or life expectancies of the participant and his or her designated beneficiary (The payments under this exception, except in the case of death or disability, must continue for at least five years or until the employee reaches age 59½, whichever is the longer period.);
- Made to a participant after a separation from service if the separation occurred during or after the calendar year in which the participant reached age 55;
- Made to an alternate payee under a qualified domestic relations order (QDRO);
- Made to a participant for medical care up to the amount allowable as a medical expense deduction (determined without regard to whether the individual itemizes deductions);
- Timely made to reduce excess contributions;
- Timely made to reduce excess employee or matching employer contributions;
- Timely made to reduce excess elective deferrals;
- Made because of an IRS levy on the plan; or
- Made on account of certain disasters for which IRS relief has been granted.

Plan sponsors should consult with their professional advisors if they are uncertain whether a particular distribution would be subject to the 10% early withdrawal penalty.

If you have questions about the information in this newsletter, or to learn more about our retirement plan solutions, talk to your SunTrust representative or call 866.786.4015 to speak with one of our strategists.

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