*Newsletter for public sector employers on compliance and best practices for today's defined contribution plans*

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News & Views

## *Message from the Consultants*

Last fall, SST merged with NFP, a nationally recognized registered investment advisory firm, to provide you with expanded services and expertise. Over the next year, our quarterly newsletter will be updated and rebranded to reflect our new relationship.

We will continue to provide information that is relevant to state and local government employers regarding their Section 457(b), 403(b) and 401(k) defined contribution retirement plans.

Two important fiduciary topics are discussed in this issue: 1) investment advisors and their fiduciary roles (page 1) and 2) 403(b) litigation and fiduciary risk (page 3). These articles are important to help you identify and understand your potential fiduciary liability and approaches that can be used to limit exposure.

Don't hesitate to contact your benefit consultant with questions on any of these topics. We are always available to help with all of your fiduciary responsibilities and decisions.

Sincerely,
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*SST Benefits Consulting*

## Investment Menu Decisions: 3(21) Advisor versus 3(38) Advisor

Selecting, monitoring and replacing investment options in defined contribution plans can be one of the most difficult and time consuming fiduciary responsibilities. For this reason, plan sponsors often seek expert, outsourced services to help with this important function.

There are two types of investment advisors offering this service that provide differing levels of fiduciary support. They are often referred to by specific sections of the Employee Retirement Income Security Act (ERISA) that applies to the fiduciary roles - Sections 3(21) and 3(38). (Note: Although public sector employers are not subject to ERISA, it generally is considered best practice guidance.)

An ***ERISA 3(21) investment advisor*** provides guidance and advice by offering recommendations to plan sponsors regarding the investment menu. The plan sponsor, however, retains responsibility for establishing the investment policy statement along with the actual decisions pertaining to the plan's investment options. Therefore, although the advisor may share this function, the plan sponsor has ultimate fiduciary responsibility for these decisions.

An ***ERISA 3(38) investment manager*** assumes full responsibility for the investment menu. The plan sponsor delegates authority to select and monitor the plan's investments and, therefore, has no responsibility for this function. This manager develops the investment policy statement and determines when changes to the fund line-up are warranted. Although the plan sponsor can never be absolved from all fiduciary responsibilities, its role is minimized under this approach.

The plan sponsor must recognize that deciding on the approach to be used in making investment menu decisions is, in itself, a fiduciary function. Whether you decide to "do it yourself" without assistance, or use a 3(21) or 3(38) approach, your decision must be based on what is in the best interest of the plan and its participants. A fiduciary best practice approach and prudent standard of care should be used in making this decision and selecting an investment advisor.

*The "Washington Insider" offers news about recent legislative and regulatory developments that may be of interest to state and local government plan sponsors*

## *Washington Insider*

### Lifetime Income Disclosure Act

The Lifetime Income Disclosure Act was recently reintroduced in the House and Senate. This bill has bipartisan support and was introduced by Representatives Luke Messer (R-IN) and Mark Pocan (D-WI) and Senators Johnny Isakson (R-GA) and Chris Murphy (D-CT). It would require employer-sponsored defined contribution plans, such as a 401(k), to provide participants with an annual statement illustrating current accumulated assets and how these amounts would translate to monthly income based on a lifetime annuity purchased at retirement.

### Senate Resolution Targeting State and City Government Run IRA Plans

The Senate recently passed a joint resolution (through the Congressional Review Act) to invalidate the Department of Labor (DOL) regulations to encourage cities and counties to establish a retirement plan for private sector workers. The regulations, which were adopted under the Obama administration, were designed to ease the ERISA burdens on payroll-deduct retirement plans offered by state and local governments by making them exempt from some of the ERISA requirements that apply to defined contribution plans offered by private sector employers. The current legislative effort, expected to be signed by President Trump, only applies to local governments (cities/counties). However, similar action regarding state-sponsored plans is expected to be taken as well.

### DOL Fiduciary Rule Delay

The DOL recently issued a press release announcing a 60-day extension to the applicability date of the final fiduciary rules released last year. The new effective date for the updated definition of fiduciary advice and the best interest standard of conduct is June 9, 2017. Further delays beyond June 9th may be initated to address President Trump's Memorandum that directed the DOL to review this rule to determine if it should be revised or withdrawn. Although the rule only impacts private sector retirement plans subject to ERISA, public sector employers will likely look to this rule to ensure they meet their fiduciary responsibilities.

### IRS Guidelines for Safe Harbor Hardship Distributions from Section 403(b) Plans

On February 23, the Internal Revenue Service (IRS) released a memorandum that lays out audit examination guidelines to determine "whether a section 403(b) plan safe-harbor hardship distribution is 'deemed to be on account of an immediate and heavy financial need' pursuant to Section 1.401(k)-1(d)(3)(iii)(B) of the Income Tax Regulations." The documentation that should be retained by the plan to demonstrate this provision is administered correctly is identified in this memorandum and includes: 1) any notifications the employer/administrator must provide to the employee; 2) general information about each withdrawal; and 3) specific details on the deemed hardship and rationale for withdrawal.

### 2017 EBRI Retirement Confidence Survey

In March, the Employee Benefit Research Institute (EBRI) released the results of the **2017 Retirement Confidence Survey**. This annual effort provides significant information about the retirement readiness of the public and private sector workforce. The findings include 60% of American workers feel very or somewhat confident about having enough money for a comfortable retirement, down from 64% in 2016. About half of respondents noted "retirement planning (53 percent), financial planning (49 percent), or health care planning (47 percent) programs would be helpful in increasing their productivity at work."

## Potential Litigation: Are plan fiduciaries at risk?

There has been increased attention in the courts on defined contribution plan costs and how they are assessed to participants. Although earlier lawsuits have focused on Section 401(k) plans subject to ERISA, recent actions have involved private university 403(b) plans, which are also subject to ERISA.

To-date, public sector plans have not been involved in these actions. However, governmental employers should consider potential implications regarding features that are similar between the university plans that are being litigated and the structure of certain Section 457(b), 403(b) and/or 401(k) plans.

This is particularly important for retirement programs that use multiple vendors (record-keepers) each with their own investment menu. The following identifies issues raised by the 403(b) lawsuits that should be examined by public sector fiduciaries.

- ✓ ***Administrative and investment costs:*** There is little guidance from the DOL or IRS as to what is considered reasonable and appropriate in regard to plan costs. As a result, this determination is up to the courts. Fiduciaries should determine if they have efficiently used their leverage and bargaining power (i.e., based on plan size) to negotiate the lowest cost for record-keeping services and investment products. Revenue sharing arrangements between providers and investment products should also be examined to determine if they produce excessive costs or inequitable fee distribution among participants.
- ✓ ***Multiple record-keepers and the process to select vendors:*** Multiple record-keepers may result in excessive costs paid by participants that would be considered unreasonable. Fiduciaries will have less bargaining power to negotiate costs because the assets are spread among multiple vendors. Also, this design results in duplication of services and products, which also can increase fees. Competitive bidding processes or benchmarking should be used to explore if the number of record-keepers should be reduced and determine the most reasonable and appropriate provider(s) for the plan.
- ✓ ***Investment products:*** As with record-keeping services, fiduciaries should use their bargaining power to secure the most appropriate class of investment products, such as institutional share class options or pooled separate accounts. Also, plans that include multiple vendors (with their own investment menu) likely have duplicate investments that dilute the plan's ability to lower fees and can result in participant confusion preventing them from making reasonable choices.

**Fee evaluation should answer…**

1) Who receives compensation from your plan?
2) What is the plan's total cost?
3) How are costs assessed to participants?
4) How are costs monitored and disclosed?
5) How do fees compare with other similar plans?

In order to mitigate fiduciaries from potential litigation, plan sponsors should maintain documentation to demonstrate decisions have been made based on fiduciary principles and best practices. Without sufficient documentation, fiduciaries are exposed to considerable risk as they will not be able to justify actions and rationale for decisions.

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