16 403(b) BEST PRACTICE TIPS:

Ignore Them at Your Own Risk

BY JIM PHILLIPS

Advisors who implement these simple, practical ideas will improve their value to their clients and have less exposure to fiduciary risk.

Whatever your motivation for being a 403(b) advisor, if you're able to develop and implement a set of best practices in the plans you serve, then everyone wins: you, the employer, the employees, and the existing participants.

The majority of our readers deal primarily with nonERISA 403(b) plans. There are, however, many employers—such as: private universities and colleges, hospitals, medical centers, and other tax-exempt organizations—who maintain ERISA 403(b) plans. We also know that after the first and second years of the Form 5500 filings, there have been approximately 19,000 ERISA 403(b) plans that filed. Of that number, only 7,200 were large plans (more than 100 participants). A conservative guess is that the estimate should be at least twice or maybe three times that number. All you need to do is think of all of the private universities, hospitals, health care centers, and other large charities out there, and there are well in excess of 7,200 of them across the United States.

It's now a common event for employers to call up their investment company or a consultant to say… "We've never filed a form 5500, we can't find a plan document, but we have had this ERISA 403(b) plan since 1987…" Where do you begin to help this employer?

This article will focus on ERISA plans and their fiduciary responsibilities. For ease of communication, we'll speak about 403(b)s as though they're all subject to ERISA and its attendant fiduciary responsibilities.

1 The first best practice is to educate your plan-level decision makers that they *are*, in fact, fiduciaries. If you're receiving compensation for providing investment advice, then you are a fiduciary as well and they should understand that. (If there is some reason you don't regard yourself as a fiduciary, you should explain why.)

2 Educate fiduciaries about their duties under ERISA. There are many, but at a minimum you should explain the *Duty of Loyalty* and the *Duty of Care*. In the most general terms, the former explains what fiduciaries must do (act solely in the best interests of the plan's participants and deliberately to promote their retirement security), and the latter explains how they must go about doing it (follow a prudent process to an expert standard).

3 Help them to understand the consequences of fiduciary breaches and prohibited transactions, which could include: fines, tax penalties, possible plan disqualification, and potential personal liability. Understanding the seriousness of fiduciary service is important to the fiduciaries, and may sharpen their efforts on behalf of the plan's participants.

What is the plan intended to accomplish? If you don't have a clear idea of where you're trying to go, what are your chances of getting there?

4 Establish a mission or purpose statement for the plan. It could be as simple as "to promote the retirement security of all eligible employees." From that statement, you can help to establish specific goals, such as to promote full participation, reasonable

contributions, and appropriate individual asset allocations.

How will you measure success? It's good to have goals, and it's important to measure a plan's progression toward those goals. We refer to these measurements as a plan's *success metrics*.

5 Determine what measurements you're going to track, what standards you're trying to meet, and what steps you'll take if you're tracking below target. These would be linked to the plan's mission or purpose, but logical metrics would likely include: participation, contribution rates, and some measurement of the rationality of participant asset allocations. If you fall short, what will you do? Will you meet with the committee to discuss additional education or communications or, perhaps, to reassess the goal?

Take an inventory of the plan. It may be some time since anyone went back and performed a thorough review of the plan, its providers, and its features. A fresh look may provide reassurance or it may identify areas that need proactive attention.

6 List all of the plan's service providers and determine who's doing what and how much they're paid. Plan fiduciaries are supposed to know this already, but many need help understanding the sometimes complicated economics beneath the surface. This is a good ramp-up for 408(b)(2).

7 Help the committee to determine the reasonableness of the compensation described above. It's a prohibited transaction to pay more than a reasonable amount. Some form of benchmarking is needed to assess reasonableness, and there are many options that can be employed depending on circumstances. These could include some form of proposal process or a third-party benchmarking report.

8 Review the plan's design. Do its features best match the plan's current needs? If it hasn't been amended or changed to take advantage of Roth, qualified default investment alternatives, or one of the auto options, should it be? If the demographics of the population have changed, should any design changes be made to reflect that?

9 Likewise, with regard to the plan provider's platform, does it offer useful features that the plan is not using? Has the architecture been opened? Do they now provide outsourcing services the plan should be using?

10 Study the demographic makeup of the employee population. Fiduciaries are obligated to consider demographics. Are the education, communication, and investment offerings consistent with the plan's age and sophistication profiles?

11 Analyze how the plan's assets are invested. Are the asset allocations suitable considering your plan demographics? Do participants have age and/or risk-appropriate individual allocations? If not, formulate a plan to improve them, possibly involving education and accessibility tools.

12 Examine the state of retirement readiness of the plan's participants. If a particular age group or other demographic has an unusually large gap, formulate a plan to improve that condition.

Plan Investments: Fiduciaries aren't held to delivering a particular level of investment return, but they are expected to act in an informed and prudent manner. Having a process in place can help fiduciaries achieve better results, and it can help demonstrate fulfillment of their *Duty of Care* obligations.

13 The plan should have a thoughtfully conceived and carefully worded investment policy statement (IPS). Legal advice is beyond the scope of this article, but the IPS should be structured enough to be useful to successive tranches of committee members, but flexible enough to avoid being "Plaintiff's Exhibit #1."

14 The menu should be well thought out and tailored to the demographic composition of the employee population, including age and sophistication characteristics. It should be right-sized for that group, allowing adequate diversification opportunities, but not overwhelming.

15 Most plans should offer accessibility help. It's one thing to offer a great menu, but getting participants to select suitable individual allocations may be quite another. Age-based and risk-based funds or portfolios can be very useful to participants, if accompanied by appropriate education.

16 There should be regular reviews and good documentation of the reviews and any decisions. The reviews should include discussion of the plan's success metrics and any actions that may be indicated.

Summing it up: The contact people at the plans you serve are probably participants as well as fiduciaries. They have two reasons to really appreciate everything you'll do to make the plan perform better.

Employees are likely to be the biggest winners if these best practices are implemented. A focus on the plan's success metrics will lead to: greater efforts to recruit new participants, stronger emphasis on making realistic contributions, and better education and accessibility tools to rationalize individual asset allocations.

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