FIDUCIARY UPDATE

Retirement plan fiduciaries should be mindful of recent compliance issues that may impact their plans.

DOL FORM 5500 CHANGES: FINAL

The DOL made several changes to the 2023 Form 5500 filing (to be filed in 2024), including:

- The participant counting methodology—which establishes whether a plan is considered large or small for audit purposes—has changed from all eligible participants to only those with account balances at the beginning of the year. The change will push many plans—403(b)s in particular—below the audit threshold, potentially saving plan sponsors time and money.
- Questions regarding compliance testing that were removed more than a decade ago were reinstated.
- New categories were added to the Administrative Expenses lines of Schedule H, including audit fees, bank or trust company fees, actuarial fees, legal fees, valuation fees, salaries, and trustee fees and expenses.

IRS REGULATIONS ON FORFEITURES: PROPOSED

On February 27, the Internal Revenue Service issued long-awaited proposed regulations on forfeitures that clarify the following:

- Forfeitures incurred under a defined contribution plan must be used within 12 months following the close of the plan year. This is less restrictive than prior informal guidance that stated that forfeitures should generally be utilized in the plan year in which they occurred.
- To ensure that forfeitures are properly utilized, recordkeepers should ideally maintain separate forfeiture accounts by plan year.
- Defined benefit plan forfeitures cannot be used to reduce required employer contributions.

BACK TO BASICS: STABLE VALUE AND GENERAL ACCOUNT PRODUCTS

STABLE VALUE FUND

Objective: Capital Preservation & Liquidity

Funds invest in high quality, short- to intermediate-term fixed income securities with perceived minimal interest rate and credit risk. They can be housed in a collective investment trust, insurance separate account, or separately managed account.

PROS:

- Underlying portfolio and crediting rate transparency
- Higher long-term yield compared to cash accounts
- Book value accounting provides for a more stable crediting rate versus money market funds
- Principal is guaranteed by wrap providers
- Lower interest rate sensitivity due to shorter duration securities versus general account products

CONSIDERATIONS:

- Liquidity constraints at the plan level, typically 12 months
- Higher interest rate sensitivity due to longer-duration securities versus money markets
- Trading constraints at the participant level depending on other funds in the plan (e.g., equity wash provisions)

GENERAL ACCOUNT OPTION

Objective: Stable Returns with Full Principal and Interest Guarantee

Investments are held in a group annuity contract that is supported by the assets of the insurer's general account (balance sheet includes insurer's liabilities, surplus, and reserves).

PROS:

- Provide attractive crediting rates relative to other product types due to longer duration securities
- Crediting rates are typically preannounced and guaranteed for a certain period
- Principal plus interest is guaranteed by insurer
- Potential to increase rates faster than stable value funds, particularly for new business

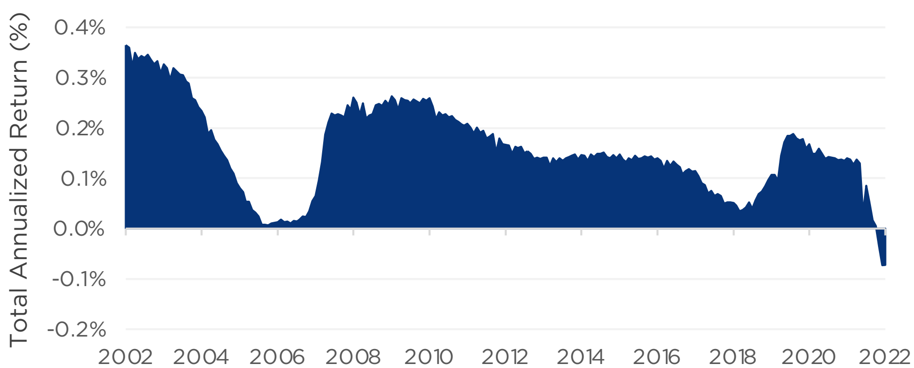
CONSIDERATIONS:

- Liquidity restrictions of five years (typically) or market value adjustment (MVA)
- Lack of portfolio and crediting rate transparency
- Guarantee is backed by the claims-paying ability of insurer
- Assets may be tied up in the event of insolvency
- Recordkeeper portability constraints

STABLE VALUE FUNDS VS. MONEY MARKET: MARKET IMPACT

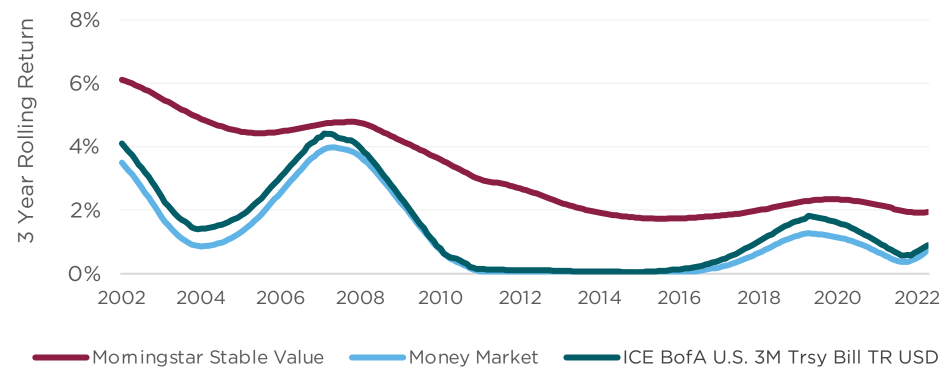
In response to high levels of inflation, the Federal Reserve rapidly increased its overnight lending rate with a series of eight rate hikes starting in March 2022. Through these hikes, the target fed funds rate increased from 0.00%-0.25% to 4.75%-5.00% as of March 2023. Short-term bonds have been most impacted by this shift in market environment, warranting an assessment of capital preservation options in retirement plans.

Stable Value Monthly Excess Return vs. Money Market



- Rapid rate increases have created an inverted yield curve where short-term bonds are yielding more than long-term bonds.
- As money market funds reinvest in higher yielding bonds, their short-term returns have exceeded stable value funds recently.

Three-Year Rolling Performance



- Money market funds hold shorter-term securities, typically one year or less, and follow changes in interest rates quickly.
- Historically, the structural advantage of stable value is that insurance wraps allow the funds to purchase a mix of short- and intermediate-term bonds while maintaining price stability for investors.

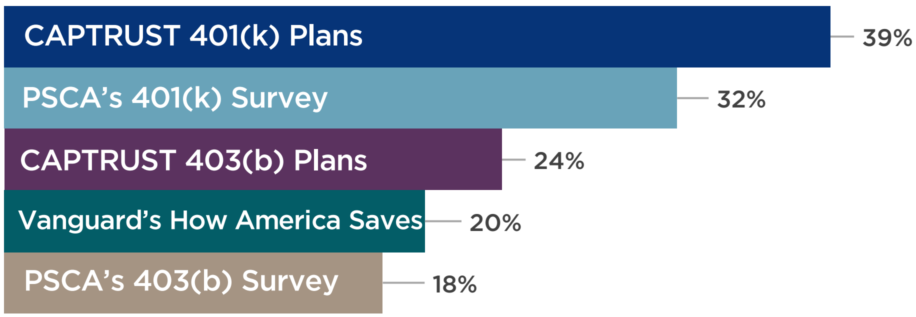
TAKEAWAYS

- CAPTRUST continues to recommend stable value funds for defined contribution plans. Over longer periods, they have delivered a higher return with less volatility than money markets.
- Stable value funds track interest rate movements over time but their movements up and down are slower by design.
- A return to a normal yield curve—where longer-term bonds yield more than shorter-term bonds—will reestablish the structural advantage for stable value funds over money market funds.

SELF-DIRECTED BROKERAGE ACCOUNT: TRENDS & CONSIDERATIONS

Under ERISA 404(a), brokerage windows—or self-directed brokerage accounts (SDBAs)—are excluded as designated investment alternatives, yet the implementation and ongoing monitoring of SDBAs are likely considered fiduciary acts and subject to ERISA. However, there is limited DOL guidance setting standards or expectations for how plan fiduciaries should evaluate, implement, and monitor SDBAs.

PERCENTAGE OF PLANS OFFERING SDBAs[1]



SDBA IMPLEMENTATION TRENDS[2]

	Percentage of Plans	
Types of Investment Options	Mutual Funds Only	Broader Options
Schwab	13%	87%
Fidelity	16%	84%
Empower	7%	93%
Maximum Allowable Percentage	Capped	Uncapped
Schwab	<10%	>90%
Fidelity	75%	25%
Empower	19%	81%

CONSIDERATIONS

EVALUATION

- Will this add value for our participants?
- Does our vendor offer different SDBA options?
- What is the brokerage provider's reputation and experience?
- What are the fees for the service?

IMPLEMENTATION

- Should a limit be placed on the types of available investments?
- Is there a need to limit certain investments for compliance or business reasons?
- Should there be a limit on the amount or percentage of assets in the SDBA?

MONITORING

- Are transaction, account, and other participant fees reasonable?
- Do our participant disclosures include general descriptions of the SDBA including fees and expenses?

CAPTRUST does not advise on self-directed brokerage accounts. The information above is intended to be educational in nature. Plan sponsors should consult their ERISA counsel for further guidance or questions related to fiduciary obligations and SDBAs.

[1] PSCA's "2022 403(b) Plan Survey," PSCA's "65th Annual Survey," Vanguard's "How America Saves 2022," and CAPTRUST Research
[2] Data represents recordkept retirement plans of all types and size from the quoted sources

FIDUCIARY FLASH TRAINING – COMMITTEE EDUCATION

Fiduciary training is a critical part of being a fiduciary and a way to minimize fiduciary risk through education and governance. The DOL views fiduciary training as an important element to managing a retirement plan and frequently looks for evidence of formal training during plan investigations. A sound fiduciary curriculum covers a range of topics—from an overview of ERISA to best practices for monitoring investments. In this installment, we cover the basics of training: who should receive it and why, recommended frequency, and available resources.

WHO

Committees and designated plan fiduciaries have a responsibility to continuously monitor and make decisions regarding the plan's investments, operations, administration, fees, and more. Providing formal fiduciary training is an effective way to ensure the committee understands its responsibility to act exclusively in the best interest of plan participants and comply with ERISA.

WHEN

New committee members should have formal training as soon as practical following their appointment. Existing committee members should receive periodic refreshers and ongoing training to build a deeper level of understanding, stay informed of current industry trends and updated regulations, and review plan-related litigation outcomes. All training should be documented in your fiduciary file.

HOW

CAPTRUST provides comprehensive fiduciary training to meet committee members' needs, including in-person training, webinars, and printed materials. Work with your CAPTRUST advisor to develop a program and cadence that best fits the needs of your committee and overall governance structure.