

## **Fixing Your 403(b) Plan: Adopting a Best Practices Approach**

*New regulations offer opportunity to create a better retirement plan for all*

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According to Spectrem Group<sup>1</sup>, approximately \$652 billion was invested in 403(b) plans as of December 31, 2006. 45% of those assets were invested in fixed annuities, 34% in variable annuities and the remainder invested in mutual funds. The majority of assets (44%) was invested through higher education programs, 26% was invested through public school (K-12) programs and another 19% was invested through healthcare programs. The remainder was invested through private school (K-12) and other programs.

On July 23, 2007, the IRS issued final 403(b) regulations, the first comprehensive guidance in 43 years. The new regulations will generally take effect on January 1, 2009. With such a large amount of retirement savings at stake, the issuance of the new 403(b) regulations is a long-awaited and welcome event in the retirement plans industry.

### **A snapshot summary of the final 403(b) regulations:**

- Written plan documents must be adopted and maintained by the employer.
- New requirements for 90-24 transfers.
- Revised testing and notification requirements for universal availability.
- Increased employer responsibilities regarding loans, hardships, catch-up contributions and required minimum distributions.
- Increased fiduciary role for the selection and monitoring of available investment options.

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<sup>1</sup> As cited on [www.403bwise.com](http://www.403bwise.com)

## **THE OPPORTUNITY IS NOW**

The final 403(b) regulations bring increased scrutiny to the operation, fee structure, and practices prevalent in the retirement plans available to our nation's teachers, health care workers, and employees of charitable and non-profit organizations. Today, plan sponsors have an exciting new opportunity to make significant contributions toward a best-practices approach to sponsoring a 403(b) plan. The end result can be a vastly improved product and service offering for plan participants.

The regulations will place new administrative duties upon plan sponsors. The good news is that there is highly qualified help available. 403(b) plan sponsors have an opportunity to leverage plan assets to attract knowledgeable and seasoned retirement plan advisors, product providers and other service vendors who can help them deliver the best retirement plan possible to their employees.

## **LEARNING FROM THE PAST: MORE IS DEFINITELY NOT BETTER!**

The most prevalent model by far in the public education sector, and in many of the 501(c)3 organizations, is the multi-provider platform. This model, which one rarely sees in the corporate sector, has developed over time in an effort to provide employees the ability to choose their investment options from a "menu" of retirement plan providers. In the past, it has not been uncommon for many well-meaning (but uninvolved) employers to have approved ten, twenty, or even fifty-plus insurance and mutual fund companies as investment providers.

The multi-provider model is flawed in two very basic ways and has produced just the opposite results that were intended. First, there have been numerous studies that show that when people are given too many choices of anything, they lose confidence (or make no decision) because the choices are overwhelming. Second, the multi-provider platform is inefficient and does not allow sponsors to leverage total plan assets and receive appropriate pricing based on aggregate assets.

## **THE ADVANTAGE OF A SINGLE-PROVIDER MODEL**

The single-provider model can alleviate the two major concerns that 403(b) plan sponsors have regarding the new regulations: greater fiduciary responsibility and increased administrative duties.

By selecting a single provider, plan sponsors can enhance their purchasing power and can negotiate lower, transparent investment fees for participants. In addition, the participants will benefit from a more manageable number of institutional-quality investment options to choose from. Participants will also benefit from customized and consistent enrollment, education and ongoing communication materials. Such a 403(b) plan can give the employer an advantage over the competition in attracting and retaining employees.

The single-provider model will also allow the plan sponsor to outsource many or all of the plan administrative responsibilities and receive accurate and timely reporting of plan activity and regular monitoring of the investment options available to participants.

### **FIDUCIARY RESPONSIBILITY: AWARENESS IS CRITICAL**

The new regulations make it clear that even plans not covered by ERISA place some fiduciary responsibilities on 403(b) plan sponsors.

There is currently much litigation and media coverage regarding fees and marketing agreements currently underway in the 401(k) arena. The 403(b) arena is not without its own litigation. One of the more high-profile lawsuits currently in existence involves the National Education Association (NEA). According to a July, 2007 article in the New York Times, the lawsuit contends that the NEA breached its duty to members by accepting millions of dollars in payments from two financial firms whose high-cost investments it recommended to its members in an association-sponsored retirement plan.

The case was filed on behalf of two NEA members who had invested in annuities sold by the two providers. It contends that by actively endorsing these products (which purportedly carry high fees), the NEA, through its NEA Member Benefits subsidiary, took on the role of a retirement plan sponsor, which must put its members' interests ahead of its own. The suit contends that by taking fees from the two providers, the NEA breached its fiduciary duty to the participants.

403(b) plan sponsors should require that the retirement plan provider accept contractually, where applicable, ERISA section 3(38) fiduciary responsibility for the selection and monitoring of a 403(b) plan's investment options.

## **FULL FEE DISCLOSURE AND AN APPLES-TO-APPLES COST COMPARISON ARE AN ABSOLUTE REQUIREMENT**

403(b) plan sponsors should require that their retirement plan providers be forthcoming and transparent regarding the fees that plan participants pay. Fiduciary responsibility requires that expenses must be reasonable in relation to the product and/or services received. And if fees are hidden, like the revenue sharing an intermediary (such as an outside advisor or plan provider) might receive from the mutual fund provider, then how does someone know if the fees are reasonable or not?

## **LEVERAGING TECHNOLOGY TO REDUCE PLAN EXPENSES**

If the plan sponsor wants to lower the cost of its plan even further, then it must assist in making enrollment and employee education more efficient. Technology is the key and needs to be used to educate and enroll 403(b) plan participants via the internet and other available media like VRS and call centers. This requires cooperation with the provider and communication to employees. Not only does this make good sense, it also provides a way for the plan sponsor to meet its obligations under the “universal availability” rule applicable to 403(b) plans.

## **CONCLUSION: IMAGINE THE POSSIBILITIES!**

Although the new regulations represent new and uncharted ground for most 403(b) plan sponsors, the opportunity exists for improved plan offerings to employees. By becoming educated and developing best practices, both employer and employee will benefit. The result will be a better retirement plan for all. And, just maybe, a better *retirement* for all.

## 5 BEST PRACTICES FOR PLAN SPONSORS

### AN ACTION PLAN

1. Form a 403(b) advisory board of five to seven members.
2. Seek out assistance from qualified outside advisory services. Employing the services of an experienced and knowledgeable retirement plan consultant or advisor can help plan sponsors in many ways:
  - Knowledge of the marketplace.
  - Education regarding appropriate fees and fee disclosure.
  - Meeting fiduciary responsibilities.
  - Written plan requirements and provisions.
  - Development of an Investment Policy Statement
  - Development and distribution of RFPs (requests for proposals); analysis and evaluation of RFP responses.
3. Review existing providers for investment performance, investment options, fees, expenses, and service standards.
4. Seek proposals from qualified retirement defined contribution plan providers (do not limit to current vendors).
5. Create standards for ongoing monitoring of the plan.

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