



The Investment Policy Statement - Time For The Annual Check-Up

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If you are like most plan sponsors, you are diligent about looking over your plan's investment line-up, analyzing relative performance, and making necessary changes as markets dictate. What is frequently overlooked, though, is the annual review of the Investment Policy Statement (IPS) after it has been approved and filed away. As with most policy documents, you should schedule a review for updating, deleting and refining the document for changing regulations and evolving best practices.

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Employers sponsor profit sharing, 401(k) and other defined contribution retirement plans to attract, retain and inspire their workers. In general, plan sponsors often develop committees that are responsible for overseeing the assets of their defined contribution retirement plans. In order for sponsors to meet their legal obligation, plan investment offerings must be prudently selected and managed. Plan

fiduciaries must also adopt and adhere to a disciplined investment process. The implementation of an IPS ensures careful consideration of both the formulation and implementation of appropriate investment strategies and outlines the responsibilities of the key players.

Every retirement plan should have an IPS that accurately reflects the specific goals and objectives of the plan. And like all fiduciary documents, it should be carefully drafted and reviewed by the plan sponsor and the plan's advisors and consultants.

In 2001, the Profit Sharing Council of America outlined what should be included in an IPS. The general topics are:

- The plan's purpose
- The purpose of the Investment Policy Statement
- The plan's investment objectives
- Roles and responsibilities
- Company management
- Investment/Benefits committee
- Benefits/Finance staff
- Investment and manage/fund selection
- Investment monitoring and reporting, benchmarking
- Investment manager termination
- Participant investment education
- Investment Policy Statement amendment process



However, many retirement plans have changed since 2001, especially with the advent of Target Date Funds, Automatic Default Options, Self-Directed Options, new benchmarks and “alternative funds.” With this in mind, highlighted below are elements that should be considered important additions to your updated IPS.

Target Date Funds (TDF) - According to the Profit Sharing Council of America (PSCA) 2008 Annual Survey, 58 percent of private employer defined contribution plans offer TDFs and 60 percent of plans with automatic enrollment have a Target Date Fund as the default investment. The selection and monitoring of an investment fund (including Target Date Funds) offered within a plan is subject to the fiduciary requirements of the Employee Retirement Income Security Act (ERISA). In particular, it’s important to remember that you must employ the same care and time selecting a Target Date Fund as you would any other fund in your lineup. By following the guidelines of the Prudent Man Rule*, you help ensure that you are following established best practices for the fund selection.

If a plan is using TDFs within its fund line-up there are several questions you should seek answers to:

- Has it been designated how the TDFs will be monitored?
- Are the funds designed to be “To Retirement” or “Through Retirement”, and how has this been communicated to Plan Participants?”
- Will the Plan use the vendor’s designated benchmark or an independent benchmark?

Finally, there are three key components used when monitoring a Target Date Fund: Its glide path, fees and relative performance (to a benchmark and to its peers.)

Glide paths between funds (the amount of equities to fixed income to cash depending upon age or retirement target dates) can vary greatly between one vendor’s

2025 fund and another’s. Is this being measured compared to other options or “peer” groups and how will this be accomplished? What happens if the funds do not perform as expected? Is the plan required by the record-keeper to utilize proprietary funds to maintain the service fees as originally quoted? Has it been disclosed how much revenue sharing is being derived from the Target Date Funds? Although these issues do not need to be completely detailed in the IPS, reviewing how the Target Date Funds will be monitored and replaced will initiate the discussion when offering TDFs in a retirement plan.

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Self-Directed Options - The Plan Document and the Service Agreement with the Recordkeeper/Third Party Administrator (TPA) are the vehicles that allow for Self-Directed or “Brokerage” options. It is important that the IPS also include language to this effect. It will determine what is allowed and/or restricted within these accounts. Most plans limit this to publicly traded companies and/or mutual funds. This is done to protect the plan from waiting on illiquid or pricing issues that could delay the filing of 5500s and other potential legal pitfalls. Other typical exclusions would include short sales, options, limited partnerships, currency trading and trading on margin.

The vendors of Self-Directed Options should be evaluated for their fees, competitive service capabilities, timeliness of trades and participant satisfaction. Wording for this evaluation should be added to the IPS.



Benchmarks - Mutual Funds and the investment industry have changed from offering the traditional nine style boxes made popular by Morningstar. Many funds offered in today's 401(k) plans are now global, all cap or specialty funds such as commodities, Real Estate Investment Trusts (REITs), or emerging markets. These are often added to provide low correlation to the traditional nine style boxes. It is important that clear and meaningful benchmarks and universes are used and updated. Often, an unbiased consultant should research appropriate benchmarks if staff does not have the internal resources for doing so. Certain mutual fund companies often will use the S&P 500 (large cap benchmark) to compare a global or all cap fund. However, in 2010, this would have been unfair and biased as emerging markets and small cap stocks almost doubled the returns of large cap stocks (the S&P 500). Many IPSs still have benchmark references to outdated names such as the Lehman Indices, which clearly indicates the document needs updating.

Advice - If the plan is offering the participants investment advice, the provider should be unbiased and the advice should be based on sound asset allocation theory and in-depth fund analysis. It should also be tailored to each participant's individual circumstances, allowing for other assets outside the plan to be considered. The advisor should be screened and reviewed in the same fashion as the selection process that occurs for the record-keeper or consultant. If the vendor/record-keeper offers it as a service, the plan sponsor should be aware of the vendor's selection process and how they avoid any conflicts of interest.

Conclusion

The implementation and continued review of a written Investment Policy Statement ensures careful consideration of both the formulation and implementation of appropriate investment strategies. The annual review of the IPS contributes to the success of an employer's defined contribution retirement program and provides the forum for the

plan sponsor and its committees to reevaluate the plan, its providers and investment options. If you haven't taken a look at your IPS lately, the New Year is a good time to start. If you feel that your IPS could benefit from a review by a fully independent consultant, the principals at Bidart & Ross can provide insight and direction regarding current trends, regulations and best practices.

About Bidart & Ross, Inc.

For more than two decades the principals and staff at Bidart & Ross, Inc. have provided Retirement Plan Sponsors, Foundation and Endowments, Family Offices, Trusts, and Corporate Assets managers completely independent and unbiased fiduciary consultancy.

For a complete overview of how we help our clients better manage their portfolios, please visit our new website at www.Bidart-Ross.com, or contact a firm principal directly:

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Footnote:

* The Prudent Man Rule applies in that a plan fiduciary must act with the care, skill, prudence and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character with like aims.