
Reviewing the investments in your retirement plan

A benefits update for executives and human resources professionals

The key to efficiently reviewing your plan's investment options is to implement and follow a systematic process at least annually.

As a plan sponsor, you should know that your work doesn't stop with the initial selection of investments for your retirement plan; ongoing monitoring and review is critical. The Employee Retirement Income Security Act of 1974 (ERISA) requires a qualified plan's fiduciary to diversify the plan's investments to reduce the risk of incurring large losses. To meet your responsibilities under ERISA, you should review the investments and documentation (such as the investment policy statement) periodically. Even if you decide to maintain your current investment mix and/or allocation, it is important to document your decisions and the supporting reasons.

As a plan fiduciary, it is your responsibility to review the choices available to participants; it is especially important given the rapid changes occurring with individual funds today. As a fiduciary, you do not have the responsibility to screen all mutual funds and find the single best investment manager. However, you do have the responsibility to make or offer prudent investments in the best interest of all participants; therefore, it is important to avoid retaining a manager who is not meeting your plan's objectives. To accurately communicate what a participant is actually investing in and to reduce overlap in the same investments, plan sponsors must understand how fund managers invest.

The key to efficiently reviewing your investment options is to adhere to a systematic process at least annually. A checklist of benchmarks can guide you through the process.

It is important to note that your review includes not only quantitative considerations but qualitative analysis as well. Some of the more important things to review include:

- Performance, including risk and return
- The fund's investment style or objective
- Personnel or manager tenure
- Investment expenses and fees

If a particular fund consistently underperforms when compared with its peer group, you may want to consider replacing it. With so many options available, how would you respond if a participant asked why you kept the fund through long periods of underperformance? If a fund underperforms for two or three consecutive quarters, you may want to take a close look at it and document your due diligence.

The key is to follow the guidelines set forth in the investment policy statement on how many quarters a fund can underperform before placing it on a watch list or ultimately replacing it.

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The fewer the fund options available to participants, the more important this review is. Finding the right number of investment options to offer participants is a balancing act. Offering too many choices creates confusion and a challenge from a communication and education standpoint. If one of the core fund's investment style or objectives change, you may want to replace the fund or add another option. For example, if your international equity investment begins to acquire domestic companies, it may require you to take action. If the fund continues to do well, you may choose to reclassify the fund and keep it. The important thing is that participants understand their options and the asset category they represent while maintaining a diversified menu.

You should carefully watch for significant changes in management, personnel, or philosophy at an investment company. For example, does the company use a "star" system (i.e., the record has been based on the talent of a single individual)? Star managers can leave for other opportunities, leaving the fund's future in question. If you are dealing with one investment management firm for all of your investments, it becomes more critical for you to review and keep up with changes in the company's key personnel and philosophy and how this may affect future performance.

In summary, it is probably impossible to determine which organizations have the best money managers; however, you can develop a process to help you maintain a group of investment options that can help prevent you from being the target of a lawsuit by disgruntled employees.

Whether you add to, replace, remove, or keep your mutual fund choices as is, it is important to follow the plan's written investment policy statement and document your efforts and the reason that supports your decision, as well as consult the plan's attorney regarding ERISA and its issues.

You can count on us

Talk to your financial professional to learn more about how we can help you conduct a review of your existing retirement plan.

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