Fiduciary Commentary

Fall 2013

north pier Fiduciary Management

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By: Brant Griffin - November 5, 2013

DOL's Fiduciary Proposal Hits Delay, Again…

The last several years have witnessed a growing movement to harmonize rules that govern the various advisory models serving qualified retirement plans. A new definition of fiduciary will attempt to create parity in the rules that govern both Broker-Dealer (BD) and Registered Investment Advisor (RIA) practices to ensure that all those providing plan advisory services are playing on a level playing field.

At issue is a regulatory environment that has not kept pace with the changes in the plan advisory marketplace. As background, the current fiduciary standard was developed by the DOL in 1975, shortly after the passage of the ERISA. The retirement plan landscape and the needs of plan sponsors have changed meaningfully since then. 401(k) plans have emerged as America's preeminent retirement funding vehicle and a plethora of advisory services supporting this evolution have been developed in response. Today, the governing standards of conduct for ERISA advisory services are antiquated, allowing divergent regulatory standards to apply depending on the organization providing the services.

Broker-dealers are subject to one set of regulations that can hold them to a non-fiduciary "suitability standard" when providing ERISA services. In most cases this low threshold standard of care does not legally obligate broker-dealers to put the interests of their clients ahead of their own. This loophole permits them to maintain practices that many would argue subordinate their client's interests. They have long been accused of hiding behind this veil to cloak the advice or guidance they provide as incidental to the inherent, transactional nature of their business. As a result, many brokers have avoided a fiduciary role with their clients and perform services that some believe, fall short. Alternatively, RIAs are subject to an elevated standard of care inherent in their legal structure. RIAs, by definition, are fiduciaries and maintain a fundamental and legal obligation to act in the best interest of their clients.

Among the concerns is that services provided by either broker-dealers or RIAs are virtually indistinguishable to most plan sponsors and participants. Slanted sales materials, industry jargon and legalese in advisory agreements simply mystify plan sponsors who are merely seeking an understanding of the marketplace and accountability for the services they seek. Due to this difficulty in distinguishing among services models, many plan sponsors often maintain a relationship with an organization without a complete understanding of the advisor's fiduciary role.

From all sides, there is a heightened sensitivity surrounding the issue of a fiduciary status today. Special interests are lining up in hopes of shaping future laws that will affect the advice that plan sponsors receive. North Pier applauds those attempting to protect the interests of plan sponsors and promote the advancement of transparency and accountability in the ERISA advisory marketplace. North Pier has always held the simple belief that every organization advising retirement sponsors, regardless of their organizational structure, should be held to a fiduciary standard. Further, every sponsor has an obligation to clearly understand the fiduciary standing of the organization hired to advise them and their plans.

The last several years has seen multiple attempts by the DOL to propose a new rule that would define what it is to be a fiduciary. The DOL's initial proposal came in 2010. At that time, Phyllis Borzi, Assistant Secretary of Labor for the

Employee Benefits Security Administration, stated there was concern that current regulations may allow plan advisors, "…from whom plans expect impartial advice, to evade fiduciary responsibility." Following several fits and starts, the DOL withdrew the initial proposal amidst fierce opposition from Wall Street brokerages houses and special interests that felt they would be adversely affected by the proposal. Earlier this year, it was once more thought a revised rule would be issued in summer 2013. Again it didn't happen.

Now, the proposal is facing road blocks once more. In October, The House of Representatives approved a controversial bill (ironically named *The Retail Investor Protection Act*) that would delay (or possibly eliminate) the DOL's authority to propose a change in the definition of fiduciary. The bill would prohibit the DOL from acting until after the SEC has finalized a similar rule to raise standards for advisors who provide retail investment advice, including to IRAs. The bill's detractors say this is a back-door attempt to undermine the investor protection provisions of the proposal. *Here we go again...*

Fidelity Target Date Series Modifies Asset Allocation

Fidelity, the industry's largest provider of target date funds with more than $170 billion under management (as of August 2013), recently announced a dramatic shift in the asset allocation of its TDF series. In a statement, Fidelity asserted that its research supported the modification and the result would better participant outcomes.

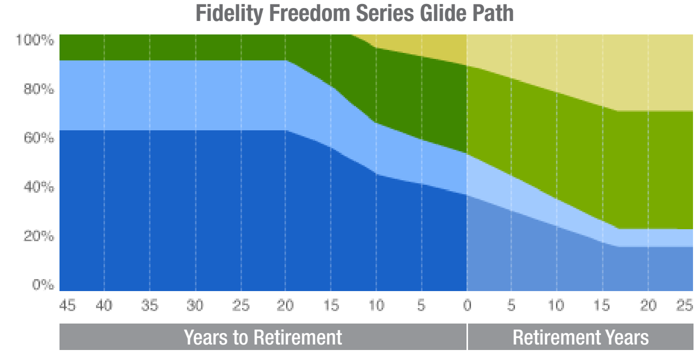
Bruce Herring, Fidelity's Chief Investment Officer for its Global Asset Allocation division said its research concluded that investors "could tolerate more equities than we thought in their retirement planning." The change also materialized due to firm's capital market assumptions, specifically for the bond market. Fidelity considered 20 years of historical returns and valuations to forecast asset class performance. The forecast did not support bonds performing as well as they have in previous years.

As a result, Fidelity's glide path for the Freedom Fund product lines and other target date retirement products will be modified to increase equity allocations across most of the portfolios, proportional decreasing other asset classes specifically fixed income. Below is an illustration of the change to the asset allocation of the Fidelity Freedom Funds Target Date 2010 product:

Fidelity Freedom Funds Target Date 2010

Asset Class	Current Targets	Projected Targets
Domestic Equity Funds	39%	43%
International Equity Funds	14%	18%
Bond Funds	39%	32%
Short-Term Funds	8%	7%

Fidelity Freedom Series Glide Path



While adjustments to the glide path or expansion of the breadth of asset classes in a TDF series is not a new concept, it illustrates the evolutionary nature of TDF products and highlights a challenge for plan fiduciaries. As TDF products evolve, how meaningful is its performance history? Perhaps due to the frequent modification of these products, historic performance comparisons are not as meaningful of a method in evaluating a TDF series and other evaluation practices should be employed.

IRS Announces 2014 Cost-of-Living Adjustments

On October 31, 2013 the IRS announced cost of living adjustments affecting dollar limitations for pension plans and other retirement-related items for tax year 2014. Many plan contributions limitations, such as those governing 401(k) plans and IRAs, will remain unchanged because the increase in the government's Consumer Price Index did not meet the statutory thresholds for their adjustment. However, other pension plan limitations will increase for 2014. Highlights include the following:

2014 Pension Plan Limitations

	2013	2014	Change
401(k) / 403(b) Salary Deferral Limit	$ 17,500	$ 17,500	No Change
Age 50 Catch-up Contribution Limit for 401(k) / 403(b) Plan Participants	$ 5,500	$ 5,500	No Change
Maximum Compensation Limit	$ 255,000	$ 260,000	$ 5,500
Social Security Taxable Wage Base	$ 113,700	$ 117,000	$ 3,300
Highly Compensated Employees			
· Compensation in Excess of:	$ 115,000	$ 115,000	No Change
Top Heavy/Key Employees			
· Officer having greater annual compensation from the employer greater than:	$ 165,000	$ 170,000	$ 5,500
415 Limits			
· Defined benifit plan dollar limit:	$ 205,000	$ 210,000	$ 5,000
· Defined contribution plan dollar limit:	$ 51,000	$ 52,000	$ 1,000

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