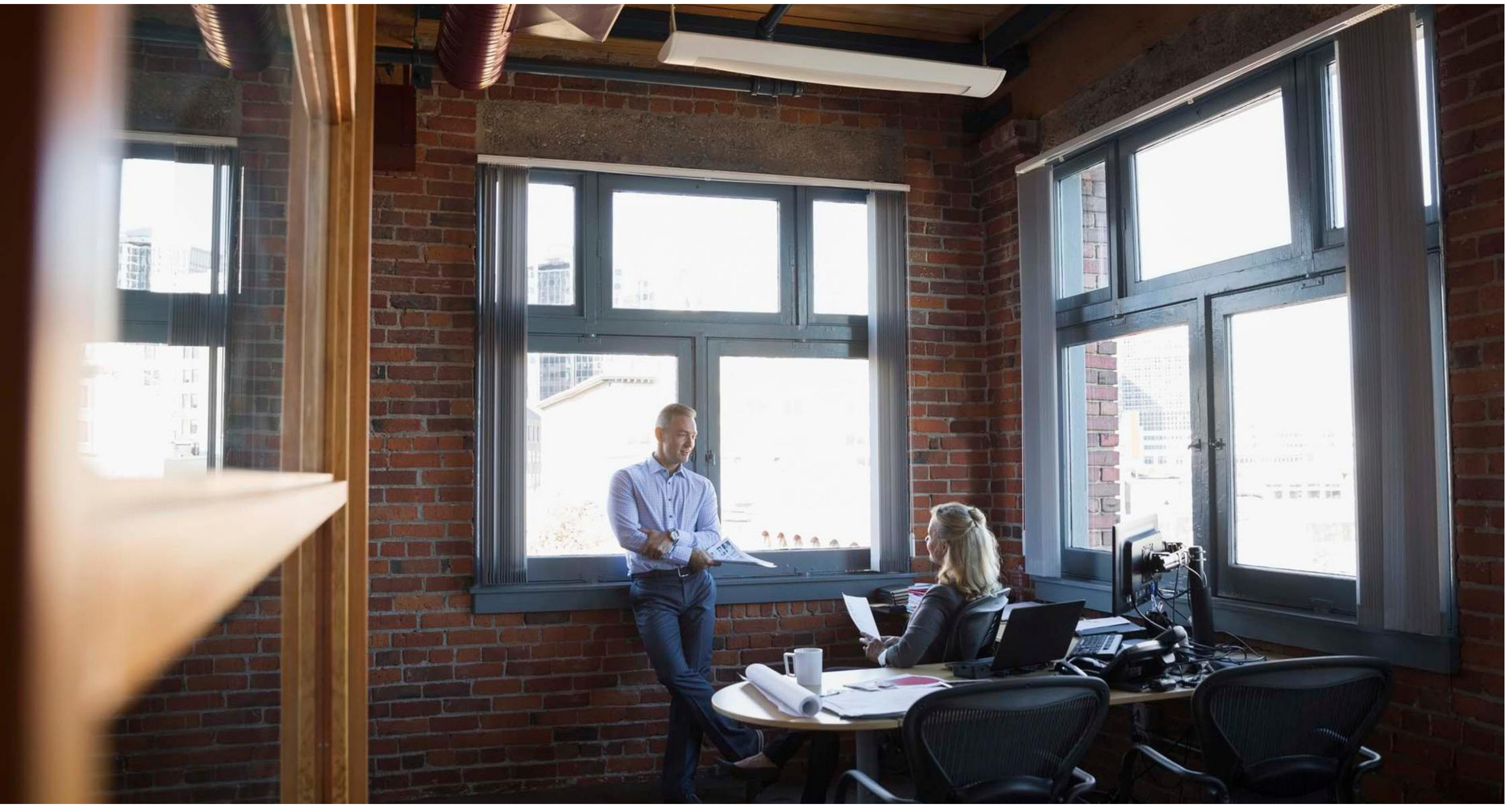

Overview of General Retirement Plan Considerations and the Role of a Plan Fiduciary

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SECTION 1

Roles and Responsibilities

Get familiar with your role as a plan sponsor, administrator, and/or fiduciary, and choices you can make to manage those responsibilities while protecting yourself and your business.

Who Is a Fiduciary Under ERISA?

The Employee Retirement Income Security Act of 1974, as amended ("ERISA") defines a 3(21) fiduciary as the person who exercises discretion, control or authority over plan assets, the management of the plan or the administration of the plan.

Though there can be a number of fiduciaries in a plan by function, ERISA requires that at least one individual or entity be named in the plan document as the "named fiduciary."

What Are a Plan Fiduciary's Duties Under ERISA?

Plan fiduciaries are subject to stringent fiduciary duties under ERISA including, but not limited to, fiduciary duties of loyalty, prudence of care to the plan.

As such, an ERISA plan fiduciary must act:

- Solely in the interest of plan participants and beneficiaries
- For the exclusive purpose of providing benefits to participants and their beneficiaries
- Discharge their duties with the care, skill, prudence, and diligence that a prudent person 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
- To defray reasonable expenses of administering the plan
- To diversify the investments of the plan to minimize risk of large losses, unless under the circumstances it is clearly not prudent to do so
- In accordance with documents and instruments governing the plan (unless inconsistent with ERISA)

In addition to ERISA, evolving Department of Labor ("DOL") guidelines will impact fiduciary responsibilities.

Examples of Persons Commonly Acting as a Plan Fiduciary Under ERISA

Fiduciaries may include:

- The business owner or plan sponsor
- The plan administrator
- The trustees of a trust holding plan assets
- A specially designated investment committee
- A properly appointed third-party service provider

Fiduciaries may be held personally liable for a breach of fiduciary responsibilities by a plan fiduciary. Plan fiduciaries often hire third-party consultants or service providers to assist with fiduciary responsibilities including:

- Recordkeeping
- Plan administration
- Investment advice
- Investment management

Trust Requirement Under ERISA and The Role of a Trustee

ERISA (generally) requires that all assets of an employee benefit plan shall be held in trust by one or more employees. The trustee(s) of a trust holding plan assets may be an individual, group of individuals or a corporation. Trustees may be named in the plan document and are responsible for administering the plan for the exclusive benefit of plan participants and beneficiaries.

Common Types of Trustees:

- Individual trustee (discretionary)
- Corporate trustee (discretionary)
- Corporate trustee (directed)

Example of Annual Reporting Requirements

Under ERISA, plan administrators are required to file Form 5500, the plan's annual financial report. The most recent Form 5500 must be made available for participant examination or provided to participants upon request.

Penalties may be imposed upon a plan administrator for failure to timely file the plan's annual Form 5500.

Components of a Qualified Retirement Plan

- **PLAN DOCUMENT:** Written document defining the retirement plan's design and benefit structure
- **INVESTMENT POLICY STATEMENT:** Where appropriate, plan fiduciaries may establish an Investment Policy Statement (IPS) that sets forth the plan's investment parameters and investment guidelines
- **A FIDUCIARY AUDIT FILE:** Organized documentation to define policies and procedures as well as demonstrate compliance and manage reporting

Fiduciary Liability Regarding Third Party Plan Service Providers

Examples of common service providers to a plan are recordkeepers, administrators and consultants. Plan fiduciaries have a duty to prudently select and monitor any service provider engaged on behalf of a plan and to ensure the fees charged for such services are reasonable.

When selecting a service provider, a fiduciary may consider the following:

- Information about the provider firm itself: financial condition and experience with retirement plans of similar size and complexity
- Information about the quality of the provider's services: the qualifications of professionals who will be handling the plan's account
- Any recent litigation or enforcement action that has been taken against the firm; the firm's experience or performance record
- A description of business practices
- The services to be provided and the proposed fee structure (including all direct and indirect fees)

Defined Roles Under ERISA

Plan fiduciaries may hire a 3(21) investment consultant and a 3(38) investment manager. Your investment advisor may serve in a 3(21) investment consultant and 3(38) investment manager capacity.

3(21) fiduciary

ERISA defines a 3(21) investment consultant as a person or entity who:

1. Renders investment advice for a fee or other compensation
2. Has or exercises any discretionary authority over the administration of the plan
3. Has or exercises any discretionary authority or control regarding management of the plan, or over the management or disposition of its assets, or otherwise
4. Exercises discretion, control or authority over plan assets, the management or administration of the plan

3(38) investment manager

ERISA defines a 3(38) investment manager as any fiduciary (other than a trustee or named fiduciary) who:

1. Has the power to manage, acquire, or dispose of any asset of a plan
2. is registered as an investment adviser under the Investment Advisers Act of 1940; is a bank; or is an insurance company qualified to perform services; and
3. has acknowledged in writing that they are a fiduciary with respect to the plan

3(16) plan administrator

A 3(16) plan administrator is responsible for the ongoing operation and day-to-day management of the retirement plan. Plan sponsors may hire a third-party administrator ("TPA") to reduce the administrative burden of operating the plan.

Functions of a Recordkeeper

The primary functions of the recordkeeper are to track the assets in a retirement plan, who is participating in the plan, how much they have invested in the plan, and in what type of assets, and any money going into or out of the plan.

A recordkeeper may perform other functions as well, such as:

- Process employee enrollment and plan participation
- Manage and track participant investments
- Provide account statements
- Manage and record 401(k) plan loan balances or hardship withdrawals

Fiduciary Bonding Requirement Under ERISA

Plan fiduciaries must have a fidelity bond and can also hold fiduciary liability insurance.

Fidelity bonds

ERISA Section 412 generally requires that every person who handles plan funds or other property be bonded to protect the plan against loss due to fraud or dishonesty on the part of persons who handle plan funds or other property.

Fiduciary liability insurance

This coverage provides protection for the insured's businesses' and employers' assets against any claim that alleges a violation of ERISA.

Plan sponsors and/or plan fiduciaries should consult their legal advisors concerning ERISA's fidelity bond requirements.

Plan Fees and Expenses

Strict rules govern which kinds of expenses can be paid from plan. Fee disclosures are required to be provided by plan service providers to plan sponsors and/or fiduciaries as well as from the plan sponsor and/or fiduciaries to plan participants.

ERISA only permits the use of plan assets to pay those benefits owed to participants under the plan and for the payment of reasonable expenses associated with administrating the plan. So while the plan sponsor must absorb so-called "settlor" expenses associated with establishing, amending or terminating a plan, plan assets may be used to pay those reasonable expenses and fees, as determined by the plan fiduciary, related to the administration of the plan, which may include reasonable fees charged by the plan's service providers.

Common Practices of Plan Fiduciaries Related to Plan Fees and Expenses

Periodically benchmarking your plan's fees is a common practice that may provide clarity on what providers are charging for servicing plans similar to yours to assist you in determining whether the fees charged by your current providers are consistent within the industry.

Request a fee disclosure document
A 408(b)(2) disclosure can be requested from your service provider to outline who is being paid using assets of the plan.

Calculate the fees paid to each service provider
Double check with your known service providers to find out who else is involved in servicing your plan.

Benchmark against industry averages
Compare plan's fees and expenses against those of other similar plans to get a sense of where your plan sits along the spectrum of service and cost.

Stay the course or choose a new provider
If you feel the plan's service provider's fees are too expensive, your Morgan Stanley Financial Advisor can help you source proposals from new service providers.

Participant Communication

Employee communication is an integral component of a plan sponsor's, plan fiduciary's and/or plan administrator's responsibilities under ERISA. Employees participating in your plan need to understand how the plan works and how their participation could affect their retirement savings goals.

ERISA imposes various documentation and disclosure requirements, including, but not limited to, the following items required to be provided to plan participants and beneficiaries:

- Summary Plan Description
- Summary of Material Modification.
- An individual benefit statement (self-directed individual account plans must provide quarterly statements)
- Summary Annual Report
- Any applicable blackout period notice
- Certain other plan-related documents must be available upon request

SECTION 2

Plan Investment Decisions and Considerations

Plan Investment Line-ups

Fiduciaries always retain responsibility for selecting the plan's investment options and for monitoring their performance. Within the investment options offered, plan participants can make selections about which funds they will invest in, and at what level.

Participant Directed Accounts

Section 404(c) of ERISA allows participants to exercise control over the investment of assets in their retirement plan accounts.

To the extent your retirement plan complies with the conditions of 404(c) and all conditions related thereto have been met, the fiduciary may be afforded relief from liability for losses that result from the participant's exercise of control over the assets in their retirement plan accounts.

Fiduciary Duties Under ERISA Regarding Plan Investment Selection and Monitoring

A fiduciary must act prudently when selecting the investment vehicles to be offered as investment options in a retirement plan's investment menu. Not only do the individual investment selection options available to plan participants need to be scrutinized carefully, the fiduciary must also ensure that the offerings are adequately diversified so as to minimize the risk of large losses (unless under the circumstances it is clearly not prudent to do so).

When determining whether an investment option is prudent for a plan, a fiduciary may consider the following (non-exclusive):

- Complying with the investment policy statement to the plan, where applicable.
- Types of underlying investments (stocks, bonds, etc.)
- Investment styles and objectives.
- Risk and return characteristics
- Historical performance
- Liquidity and future cash flows
- Fund manager (tenure, style)
- Fees and expenses

During the investment selection process, plan fiduciaries are required to make such investment selections based on suitability of each investment option evaluated and in accordance with the fiduciary standards under ERISA. Further, the fiduciary must monitor each investment on an ongoing basis. Consider whether a carefully crafted investment policy statement may assist the plan fiduciary in clearly identifying investment goals.

How Do Fiduciaries Make Prudent Investment Decisions?

Prior to selecting the investment options for the plan, the Investment Committee should outline specific screening guidelines, by category, that each of the investment options must meet. A process for selecting investments may include consideration of a variety of statistical and non-statistical factors, such as:

- Investment objectives
- Performance relative to its index and peer group
- Risk characteristics
- Investment style
- Fees (including expense ratios and other potential costs, such as redemption fees)
- Manager tenure
- Style consistency
- The degree of correlation with other plan investment options

How Can Fiduciaries Monitor Retirement Plan Investments?

Consider the following in your process for monitoring plan investments:

- Establishing objective criteria to effectively measure investment performance
- Identifying criteria that may be used in considering whether to replace an investment vehicle, such as:
  - Fund manager changes and/or changes in fund company ownership
  - Performance and risk relative to appropriate benchmarks
  - Performance in varying market conditions
  - Portfolio changes and/or style consistency
- Reviewing regular reports describing the performance of the investments

Qualified Default Investment Alternative

You can establish a default plan investment option known as Qualified Default Investment Alternatives ("QDIAs"), which is used as a default investment option under the plan where a participant does not make an affirmative investment selection.

Conditions to establishing a QDIA under a plan:

- Invest assets of the participant's account in the plan's QDIA
- Give participants an opportunity to provide investment direction, employing QDIAs when participants fail to provide such direction
- Provide participants with a notice identifying the plan's QDIA in advance of the initial investment and annually thereafter
- Send participant investment information on the QDIA, such as prospectuses
- Give participants the ability to direct investments out of the QDIA as frequently as from other plan investments, but at least quarterly
- Ensure that fees for the QDIA are not greater than those that would have otherwise been charged to participants using that investment option
- Offer a "broad range of investment alternatives" as defined in the regulations under section 404(c) of ERISA

QDIA Requirements

- A mix of investments that takes into account the individual's age or retirement date (e.g. a target date fund)
- An allocation among existing plan options based on individual's age or retirement date
- A mix of investments based on characteristics of the group of employees as a whole (e.g. a balanced fund)

Note that there are restrictions on QDIAs, including:

- A capital preservation product may be used for only the first 120 days of participation
- QDIAs generally may not invest participant contributions in employer securities
- Stable value funds DO NOT qualify as a QDIA for new contributions

SECTION 3

Plan Administration Considerations

Help manage the health of your plan over time by testing for nondiscrimination, monitoring staffing changes and carefully documenting plan policies, procedures and compliance.

What is Nondiscrimination Testing?

There are three nondiscrimination tests that may be utilized for purposes of the nondiscrimination requirement that may apply to your plan type (such as a 401(k) plan) to consider: the Top-Heavy Determination, Actual Deferral Percentage ("ADP"), and the Actual Contribution Percentage ("ACP") tests. Here are key considerations of each test:

1. **TOP-HEAVY DETERMINATION:** The Top-Heavy Determination test under Section 416 of the Code is used to identify plans where key employees own more than 60% of plan assets. These top-heavy plans generally require company contributions for all non-key employees that participate in the plan equal to 3% of their annual compensation for the plan year.

2. **ACTUAL DEFERRAL PERCENTAGE:** ADP tests pre-tax and after-tax deferral contributions, excluding catch-up contributions, for nondiscrimination. The ADP test requires the average contribution rate of highly compensated employees for that year does not exceed the greater of 125% of the average contribution rate for non-highly compensated employees, or the lesser of 200% of the non-highly compensated employee average rate or such average rate plus 2%.

3. **ACTUAL CONTRIBUTION PERCENTAGE:** ACP tests use the same methodology as the ADP test on matching and voluntary after-tax contributions for nondiscrimination.

What is a Fiduciary Audit File?

A Fiduciary Audit File may help plan sponsors and plan fiduciaries understand, manage and demonstrate compliance with their fiduciary responsibilities.

Many parties have the right to file suit to seek applicable remedies for fiduciary breaches under ERISA, including plan participants, other plan fiduciaries, and DOL. Given this risk of exposure and the many legal requirements imposed on plan fiduciaries under ERISA, it is critical to be diligent about compliance with you fiduciary responsibilities.

A Fiduciary Audit File may help:

- Organize plan records
- Identify areas requiring further development
- Demonstrate that plan policies and procedures were established, maintained and periodically reviewed
- Document adherence to those policies and procedures
- Manage plan administrative or investment issues more effectively
- Prepare for and respond to participant or government inquiries

SECTION 4

Summary of Common Plan Design Features and Considerations

Automatic Enrollment

Automatic enrollment automatically enrolls an eligible employee in their employer-sponsored retirement plan, which may help employees follow through on what they might not do on their own, namely, to join a retirement plan.

As more employers confront the reality that employees may not be adequately saving for retirement, the popularity of 401(k) plan automatic enrollment plan design features continues to grow.

Research conducted by Defined Contribution Institutional Investment Association (DCIIA), revealed that 89% of respondents surveyed reported an increase in employee participation as a result of implementing auto features in a defined contribution plan.[1]

When considering incorporating an automatic enrollment plan design feature, consider the plan's objectives for offering automatic enrollment, the costs of matching contributions for the population of eligible employees to be automatically enrolled and any impact to the plan's nondiscrimination testing requirements.

Beginning in 2025, newly-established 401(k) and 403(b) plans are required to automatically enroll eligible participants. In general, unless an employee opts out, a plan must automatically enroll the employee at an initial contribution rate of at least 3% of the employee's pay and automatically increase the initial contribution rate by one percentage point each year until it reaches at least 10% of pay.[2]

Each type of automatic enrollment arrangement has specific notice requirements. Prior to adding automatic enrollment plan feature, plan sponsors should consult their legal advisors.

Examples of Commonly Used Automatic Enrollment Plan Design Features

Consider these three common automatic enrollment designs: the Basic Automatic Contribution Arrangement ("ACA"), the Eligible Automatic Contribution Arrangement ("EACA"), and the Qualified Automatic Contribution Arrangement ("QACA").
In each arrangement, participants may opt out of having contributions deducted from their pay or may change the percentage of pay being automatically deducted at any time.

Basic Automatic Contribution Arrangement (ACA)

This is the most basic automatic enrollment arrangement and easiest for plan sponsors to implement. The plan document specifies the percentage of wages an eligible employee will have automatically deducted using the ACA design feature. Under a plan meeting the requirements of the ACA feature, eligible employees are automatically enrolled in the employer's plan unless they affirmatively elect to opt out.

Eligible Automatic Contribution Arrangement (EACA)

This arrangement is similar to the basic ACA design, but includes several additional requirements including, but not limited to, the following:

- Eligible employees must uniformly contribute the plan's default percentage after being provided with written notice of their auto-enrollment in the plan
- Employees must be permitted to withdraw their automatic contributions and earnings (within 30 -90 days after the employee's first automatic enrollment contribution was withheld from wages) in accordance with process prescribed under the terms of the plan document
- Upon becoming eligible to participate, employees are immediately 100% vested in their automatic contributions

Qualified Automatic Contribution Arrangement (QACA)

This QACA plan design feature includes a safe harbor provision, which may benefit plan sponsors by exempting the plan from nondiscrimination testing requirements that would otherwise apply to the plan.

In exchange, plan sponsors must adhere to the following requirements:

- Plan must include an auto-escalation design feature, which requires uniform minimum default automatic contribution percentages starting at 3% and gradually increases each year an eligible employee participates
- Mandatory employer contributions made at a minimum of either matching contribution of: 100% of an employee's contribution up to 1% of compensation and a 50% matching contribution for the employee's contributions above 1% of compensation and up to 6% of compensation; or a nonelective contribution of 3% of compensation to all participants, including those who choose not to contribute to the plan
- Employees must be 100% vested after no more than 2 years of service

Auto Escalation Feature

Plan designs that incorporate automatic escalation features that seek to increase participant contribution rates regularly over time may consider including automatic enrollment plan design features to achieve contributions on par with voluntary designs.

Plans that add an automatic escalation feature must also establish a maximum contribution rate at which increases will stop. To determine your rate cap, consider evaluating the benefits that a higher cap could have on the retirement income adequacy of your employee base.

Consider determining the auto-escalation rate that makes sense for your plan participants when considering including an auto-escalation design feature in your plan.

Designated Roth Account Plan Design Feature

While the advantages of having contributions allocated to a designated Roth account under your plan may not be realized for years, participants may benefit in the form of tax-free distributions if certain conditions are met.

The IRS allows plans that permit and accept contributions to a participant's designated Roth plan account to specify that automatic enrollment contributions be made on a Roth basis.

Since plan participants are likely to be in a lower tax bracket today than in the future, lower-income employees stand to benefit the most from the potential advantages of a Roth designated plan account. Evaluate your employee base to determine what best advantages them for retirement.

Adhering to fiduciary responsibilities can be a full-time job, however, you don't have to do it alone. Your Morgan Stanley Financial Advisor can help you comply with your fiduciary investment-related duties under ERISA.

1 https://cdn.ymaws.com/dciia.org/resource/resmgr/resource_library/DCIIA_RRC_Plan_Sponsor_Surve.pdf, page 7.

2 This requirement generally applies to 401(k) and 403(b) plans established after Dec. 29, 2022, the date the SECURE 2.0 Act became law, with exceptions for new and small businesses, church plans, and governmental plans. (Source: IRS.gov)