

University Of Washington  
Faculty Council on Benefits and Retirement  
2:30 p.m. – 4:00 p.m., May 20, 2013  
36 Gerberding

**Meeting Synopsis:**

- 1) Call to Order
- 2) Review of the Minutes from April 22, 2013
- 3) Healthcare Plans
- 4) Discussion on UWRP Plan to Pay Independent Investment Advisors
- 5) Adjourn

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**1) Call to Order**

The meeting was called to order at 2:30 p.m. by Chair Emery.

**2) Review of the Minutes from April 22, 2013**

The minutes from April 22, 2013 were approved as written.

**3) Healthcare Plans**

Kathleen Dwyer explained that it will be better to discuss this agenda item during the Fall Quarter as the state is still developing a new health care exchange. The agenda item will be delayed until the Fall Quarter.

**4) Discussion on UWRP Plan to Pay Independent Investment Advisors [Exhibit A]**

Kathleen Dwyer discussed a request to the University to use UWRP plan assets to pay independent investment advisors. There are two questions being considered by the UWRP/VIP Fund Review Committee that Dwyer wanted to bring to the attention of the FCBR:

- What options are available for UWRP and VIP participants to obtain investment advice?
- Should UW Allow payment of individual advisor fees from the UWRP/VIP plan assets?

*UWRP and VIP*

Currently the authorized UWRP and VIP recordkeepers, Fidelity Investments and TIAA-CREF provide “guidance” which is considered general financial and investment education. The term “guidance” is used carefully to indicate the advisor is only providing education and is not responsible for a client’s investment strategies. Investment “advice” goes beyond “guidance” and provides specific investment recommendations. Currently, investment advice is not available with UWRP and VIP. However guidance provided by Fidelity provides “one click” implementation, which makes it very easy for participants to implement any guidance provided.

Discussion moved to managed accounts. A managed account allows the investment advisor to create a portfolio for the participant and implement the portfolio on an ongoing basis. Managed accounts are not offered through the plan, and in order to allow it the plan (the UW) must elect to have this service

offered and a Request for Proposal may be required. One important note is that an asset-based fee to participants would apply.

Third-party fund trading is allowed by the Plans, which allows the participant to authorize a financial advisor or other party to make transactions on his/her behalf. For example, one person in the family will manage the investment for their spouse/partner with their access. Any payment for this service is currently made outside the retirement plan.

#### *Registered Investment Advisor*

A Registered Investment Advisor (RIA) is registered with the SEC or state regulatory agency for the purpose of providing financial advisory services to others. RIAs have fiduciary responsibilities, and if allowed in the plan, would be considered service providers of the plan. Fees for the service provider could be paid out of plan assets. Agents of the RIA have to pass key exams in order to offer financial advice, and to be considered for payment via a recordkeeper an RIA designation is required.

#### *Fidelity*

Fidelity currently offers investment guidance, not advice. They do provide a portfolio review which sounds like advice, but does not constitute “advice” based on the definition. The portfolio review provides a suggested “model portfolio” using the plan’s investment options and provides an action plan for participants. Managed accounts are available to participants but not through the UW. If UW were to select the service an asset-based fee would apply. When third-party trading was originally authorized UW decided not to allow RIAs to deduct fees from plan accounts. Fidelity does have a business acceptance process for RIA agents but does not receive compensation from the service.

#### *TIAA-CREF*

TIAA-CREF provides financial consultants to provide general investment guidance on UW plan assets. Wealth management advisors are also available which provide guidance to utilize the five open annuity options. TIAA-CREF offers employers two options to provide investment advice:

- Participant choice – Participants can work with any RIA agent. Fees paid out of plan assets can be capped at 2 % or lower.
- Advisor network – This new product ensures that participants are only working with advisors who have been pre-screened against industry standards. Fees paid out of plan assets are capped at either 1.25% or 1%. This is a brand new option with no history and only one institution has signed up for this.

#### *Legal Issues*

The question is whether there can be sufficient supports in place to provide guidance for participants and assist them in a safe environment since there are issues with the financial planning industry. The Pension Protection Act of 2006 requires that the process of choosing an advisor avoids self-dealing and conflicts of interest. The Department of Labor requires that investment advice, in order to be compliant with the Employee Retirement Income Security Act (ERISA), must be unbiased and objective. The IRS has provided that fees paid to an RIA from a participant’s retirement accounts will not be treated as a

taxable distribution if several conditions are met. While ERISA does not apply to UW, it does follow many of the aspects of ERISA that protect participants.

#### *Asset Payments to Third-Parties*

UW is currently awaiting data from other institutions. At Fidelity, 50% of 403(b) participants allow RIAs to deduct fees from their plans. At TIAA-CREF, a few hundred non-ERISA plans allow this form of payment while only a few are ERISA plans.

#### *Pros and Cons*

There are several pros and cons the UW must consider when deciding whether or not to allow deduction of RIA fees from participant accounts. Pros to such a change may allow participants to:

- Maintain their existing relationship with an advisor
- Facilitate the use of investment advice
- Pay fees with pre-tax dollars
- Allow assets outside the plans to be considered through RIA and managed accounts

However, the cons include:

- Limited or no oversight of the fee arrangement
- UW may be challenged if “unreasonable fees are charged”
- There would be limited ongoing review unless acted upon by the participant
- Participants would be on their own to select RIAs

#### *Discussion*

Any changes to UWRP and VIP Plan Documents will have to be approved by the Board of Regents. There will be a discussion at the Fund Review Committee and they will likely make a recommendation to the Provost. In addition to the FRC input, the Provost will want feedback from the FCRB. One question to consider is if UW could mitigate liability with a “waiver of liability” signed by participants.

A question was raised asking if benefits would be reduced if the state decided to tighten the budget. The state does contribute to the plan as an employer and it is up to the legislature to decide what happens. The state caps use of state funds for the employer contributions to 6% and UW makes up the difference. It is also important to keep aware that the legislature has been scrutinizing UW retirement plans in recent years. .

This agenda item is being addressed now in response to a member on FCBR who requests that the UW approve payment of advisor fees from Plan Assets. The item was put on hold until recordkeeping change was completed and slated for the end of the current academic year to be discussed.

Discussion ensued regarding individual choice versus institutional control:

Comments from FCBR members: If changes are made then the fee for personal investment advice would be pretax, come out of a participant's investment account, and paid directly to the advisor. A key change is the fee will not be treated as taxable event. Dwyer clarified that the fee will be considered tax exempt, not tax deferred. However, from a benefits point of view this may be troubling because people do not pay much attention to their quarterly statements. Concern was raised about employees becoming inundated by requests from investment companies. Discussion ensued. People tend to put retirement plans on autopilot and it is good to develop a relationship with a good advisor and discuss investments. The product through Fidelity is very close to investment advice, and for \$50 a year, it is a great tool to have.

Concern was raised that financial planners are restructuring portfolios in confusing ways and taking lots of money from participants. Participants are easily sucked in and financial planners are taking as much as 2-3% of gained assets. This is a large chunk of money and the main concern is the percentage rate that participants are charged. Discussion ensued regarding fiduciary responsibilities, investing and index funds.

A question was raised asking what needs to happen if FCBR wants to make a recommendation to the Provost. The Fund Review Committee will be meeting to discuss this and may feel compelled to address the issue. Additionally, the Provost will want to know FCBR's position. Discussion ensued regarding the process. Discussion moved to the Board of Regents and their role and understanding of benefits and retirement.

FCBR is tasked with making recommendations that benefit the majority of the employees of the UW. Discussion ensued. The changes will only impact whether advisor fees are charge pre-tax or after-tax. Discussion moved to determining if this fee is considered a business expense, if it can be deducted from total income, and IRS rules. If a participant already hires an outside advisor the only difference is that the money comes out of the plan. Concern was raised that fees would be charged on autopilot and people do not pay attention to their quarterly statement. Discussion ensued.

One thing the UW could do is develop a strong statement that prevents financial planners from aggressively crawling over campus searching for clients. While that is a good idea, it is important to be aware of UW's current policy on inviting financial planners to educate colleagues on campus. Financial planners typically recruit clients through these "educational presentations", but this should not happen on campus because it is using UW time and resources.

A question was raised whether to make a decision on this now or wait for the Fund Review Committee to make their recommendation. The Fund Review Committee will take this issue very seriously and would likely consider any feedback that it receives. A question was raised asking if FCBR has fiduciary responsibilities. Discussion ensued. Emery stated he wants to get the Fund Review Committee's feedback first before acting on this issue.

*Discussion on Opt-in/Opt-out changes at SCPB*

The Senate Committee on Planning and Budgeting (SCPB) will be discussing opt-in/opt-out issues at their next meeting. The Provost has requested that the discussion slow down a bit in order to take a further look. SCPB will hold off for now in order to assess the legal questions and issues, including concerns with the ramifications of the proposed changes, grandfathering individuals already participating, movement within the plan, and compliance with IRS regulations. Dwyer asked for FCBR's feedback. This process takes a little longer but SCPB will try to have this back on the agenda by the Fall Quarter.

## 5) Adjourn

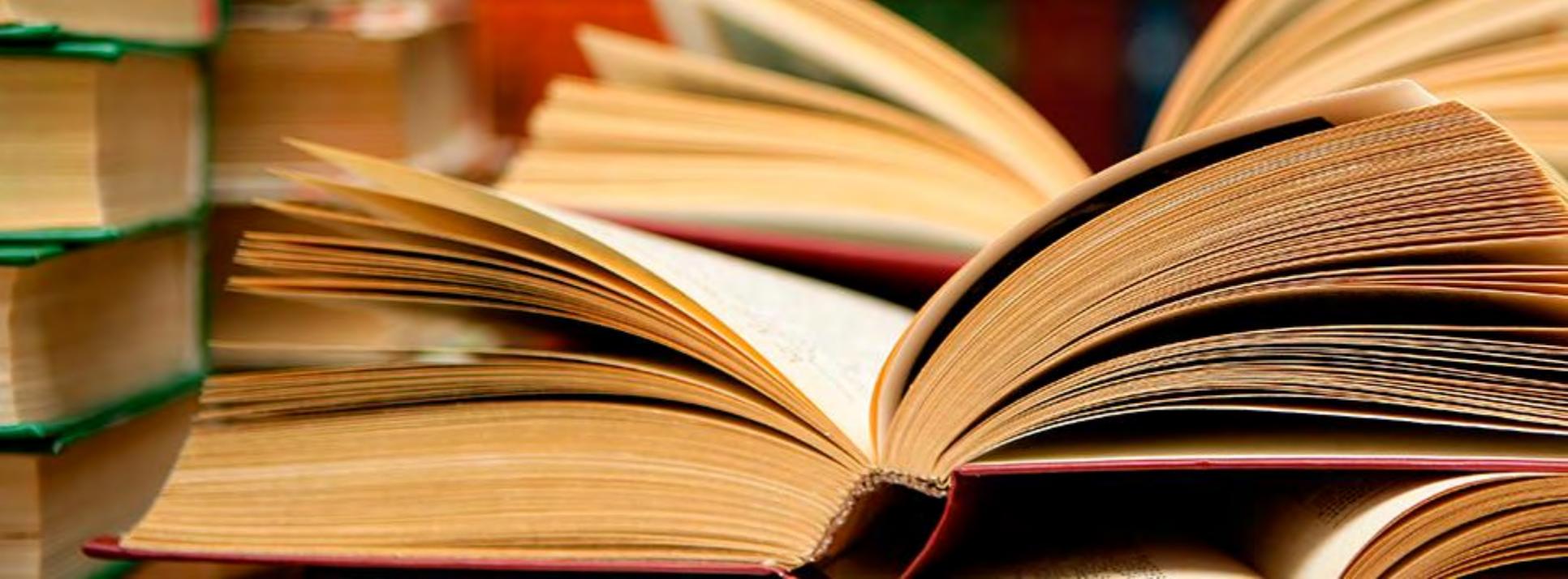
The meeting was adjourned at 3:50 p.m. by Court (Emery left prior to adjournment).

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*Minutes by Grayson Court, Faculty Council Support Analyst, gcourt@uw.edu*

**Present:**           **Faculty:** Emery (Chair), Breidenthal, Nowell, Govin, Mittler  
**Guests:** Kathleen Dwyer  
**Ex-Officio Reps:** Bowen

**Absent:**           **Faculty:** Nihan, Holt  
**President's Designee:** Kornberg  
**Ex-Officio Reps:** Navarrete, Glenn, Deardorff



University of Washington | May 2013

## **Investment Advice**

### **Use of Plan Assets to Pay Independent Advisors**

To protect the confidential and proprietary information included in this material, it may not be disclosed or provided to any third parties without the approval of Aon Hewitt.

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# Questions

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What options are available for UWRP and VIP participants to obtain investment advice?

Should UW allow payment of fees for this advice from the UWRP/VIP plan assets?

# University of Washington RP and VIP

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- Investment *guidance* **is** available
  - General financial and investment education
  - Asset allocation modeling
  
- Investment *advice* **is not** available
  - Goes beyond investment guidance
  - Provides specific investment recommendations
  
- Managed accounts **are not** offered
  - Investment advisor creates a portfolio for the participant and implements the portfolio on an ongoing basis
  - The plan must elect to have this service offered and an RFP may be required
  - Asset-based fee to participants would apply
  
- 3<sup>rd</sup> party fund trading is allowed
  - Participant authorizes the entity to transact on his or her behalf
  - Anyone can be designated by the participant to trade on their behalf (spouse, partner, advisor, etc.)
  - Any payment for services are currently outside the retirement plan

# RIAs

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- Registered Investment Advisor (RIAs) are individuals or firms who have registered with the SEC or state regulatory agency for the purpose of providing financial advisory services to others
  - Investment advisors are considered a fiduciary to their clients
  - Investment advisors would be considered service providers of the plan
  - Fees for plan service providers can be paid out of plan assets
  
- RIA registration
  - In general, RIAs managing assets totaling less than \$100 million must register with the state securities agency in the state where they have their principal place of business
  - In general, RIAs who manage \$100 million or more in client assets must register with the U.S. Securities and Exchange Commission (SEC)
  
- RIA exam requirements
  - Agents of the RIA who are charged with providing investment advice are called an "Investment Adviser Representative" (IAR).
  - IARs must generally complete The Uniform Investment Adviser Law Examination (Series 65)
    - Exam waiver requirement can be met by holding a pre-qualifying designation: CFP, ChFC, PFS, CFA, or CIC
  
- To be considered for payment via a recordkeeper (as described later), an RIA designation is **required**.

## Background on Fidelity

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- Investment *advice*
  - Not currently offered by UW
  - However, Fidelity offers an investment *guidance* service (“Portfolio Review”)
    - Provides a suggested model portfolio using the plan’s investment options
    - Provides an action plan for participants including “Click-to-trade” functionality
  
- Managed accounts
  - Not currently offered by UW
  - But are available through Portfolio Advisory Services at Work (PASW) or Financial Engines
    - UW would likely be required to post an RFP to select a service
  - Asset-based fee to participants would apply
  
- Registered Investment Advisors (RIAs) access is available on the UW plans via 3<sup>rd</sup> party trading
  - When 3<sup>rd</sup> party trading was authorized, UW opted to *not allow* RIAs to deduct fees from plan accounts
  - Fidelity has a business acceptance process for RIA firms/individuals
    - Otherwise, no screening or monitoring
  - Fidelity receives no compensation for this service

## Background on TIAA-CREF

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- Online investment advice and managed accounts
  - Not available to UW
  
- TIAA-CREF Financial Consultants – currently available
  - For more straightforward financial needs
  - Provides general investment guidance (asset class recommendations) on UW plan assets
  - Guidance only - utilizes the 5 open annuity options
  - In person or via phone
  - No extra fee applies
  
- Wealth Management Advisors (WMAs) – currently available
  - For those with large accumulations (such as \$500K or more) and specialized situations
  - Guidance only - utilizes the 5 open annuity options
  - No extra fee applies

## Background on TIAA-CREF

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- Access to independent Registered Investment Advisors (RIAs)
  - Not offered by UW
  
- TIAA-CREF offers employers two options to provide investment advice through RIAs:
  - Note: UW may need to post an RFP to select such services
  - “Participant Choice”
    - Participants can work with any SEC or state-registered investment advisor as long as they are in good standing with the appropriate federal or state regulatory agencies and are operational with TIAA-CREF’s Advisor Services.
    - Fee paid out of plan assets can be capped at 2% or lower
  - “Advisor Network”
    - Allows plan sponsors to ensure that participants are only working with those advisors that have been prescreened against industry-minimum standards
    - Utilizes unaffiliated firm (Fiduciary Risk Assessment) to perform selection/monitoring
    - Screening criteria includes: Experience, Assets, Fee Structure, Investment Policy, Disciplinary History, Insurance Coverage, Code of Conduct
    - Newly available – only 1 plan has been implemented
    - Fees paid out of plan assets capped at either 1.25% or 1%
    - Advisors pay a fee to FRA for the initial screening and ongoing review
  
- TIAA-CREF receives no compensation for this service

# Legal Background

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- Pension Protection Act of 2006 (PPA)
  - The process for choosing an advisor must avoid self-dealing and conflicts of interest
  - PPA provided two exemptions from ERISA's prohibitions on self-dealing:
    - The investment advice provided is based on a computer model certified as unbiased and as applying generally accepted investment theories, or
    - The adviser is paid on a "level-fee" basis (fees do not vary based on investments selected)
  
- Department of Labor (DOL)
  - In order to avoid violating ERISA, investment advice must be unbiased and objective
  - The process for choosing an advisor must avoid self-dealing and conflicts of interest
  - The fees must be reasonable
  
- Internal Revenue Service (IRS)
  - The IRS has provided that fees paid to an RIA retained by a participant and paid from participant retirement accounts will not be treated as a taxable distribution if certain conditions are met:
    - The plan treats these fees as plan expenses
    - The payments are for expenses that are ordinary and necessary
    - The payments are only made from accumulations in the participant's retirement account
    - The services of the RIA must be provided through a formal arrangement

## Legal Background

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- If UW were subject to ERISA, the plan fiduciaries would be held responsible for the choice of investment advisors, if compensation is paid from plan assets
- ERISA does not apply to UW, but there might be state trust laws or other laws that would apply
- UW follows many “best practice” aspects of ERISA (Plan Document; spousal consent; quarterly statements, fee disclosure, etc.).

# Prevalence

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- Who currently allows third party payments from plan assets?
  - Awaiting data from other higher education institutions
  - Fidelity plans
    - For multi-vendor, non-ERISA, higher-ed plans, about 50% allow RIAs to deduct fees
    - For ERISA plans exclusive with Fidelity, the ability to have RIA fees deducted is fairly low
  - TIAA-CREF plans
    - A few hundred non-ERISA plans allow this
    - Few are ERISA plans
  - Online investment advisory services such as Financial Engines are more prevalent at ERISA plans (39% of defined contributions plans according to Aon Hewitt data)
    - Consistent process, but less customizable and less personal
    - Often do not advise on assets outside of the plan

# Pros and Cons of Deducting RIA Fees From Participant Accounts

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- Pros
  - May help facilitate the use of investment advice, which could help participants create appropriate portfolios for their individual circumstances
  - Participant may already have an existing relationship with an advisor and now the RIA can manage these retirement plan assets and the participant can pay those fees with pre-tax dollars
  - RIAs and managed accounts can consider assets from both the Fidelity and TIAA-CREF platforms as well as assets outside of the Plans
  
- Cons
  - Fee arrangement is between the participant and the advisor with limited or no oversight and review from the sponsor (UW) or the recordkeeper
  - UW may be challenged if “unreasonable fees” are charged to a participant from plan assets
    - UW would need to review legal options to obtain a waiver of liability
  - Even though there is a registration process, there is limited ongoing review of the RIA except what may be done by the individual participant in hiring and continuing to work with the advisor
    - Investment process is not consistent across RIAs
    - Can create some fiduciary concerns for ERISA plan sponsors, not knowing who’s deducting fees and for what services
  - Many RIAs may have a minimum asset requirement
  - Participants are on their own to identify and select the RIAs

## Comparison of RIAs with Managed Accounts

	<b>RIAs</b>	<b>Managed Accounts</b> (e.g.) Financial Engines)
<b>Fees</b>	1% to 2% of plan assets per year	0.35% to 0.65% of plan assets per year
<b>Investment Advice Consistency</b>	Less consistent – advice will vary significantly by RIA	Consistent advice for similar participants
<b>Investment Advice Customization</b>	High  Some RIAs will have expertise to effectively integrate TIAA-CREF annuities into their analysis	High  Would need to be evaluated as to how TIAA-CREF annuities are factored in to the process
<b>UW Liability</b>	Unclear. Employers cannot provide effective screening/monitoring of individual RIAs.	Very low – due diligence via RFP process provides appropriate screening.
<b>Account size minimums</b>	Varies by RIA	None

## Other Points to Consider

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- Requires change to UWRP and VIP Plan Documents, with approval by Board of Regents
- State of Washington PERS 3 / TRS 3 defined contribution plans do not allow participants to access plan assets prior to retirement
  - Will this be viewed as an in-service withdrawal by the state of Washington?
- Question: Could UW mitigate liability with a waiver of liability signed by participant?

## ERISA Rules on Prohibited Transactions – Additional Information

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- ERISA prohibits a variety of transactions with a “party in interest”
  - A “party in interest” includes
    - Plan sponsor
    - Plan fiduciary
    - Plan service provider
  - The transactions that are prohibited include
    - Transfer of plan assets to a party in interest
    - Use of plan assets by or for the benefit of a party in interest
    - Lending or extension of credit between plan and party in interest
  - Potential sanctions include
    - Obligation to undo the transaction
    - Monetary penalties
    - Excise taxes
  - Exceptions to the prohibited transactions rules for certain transactions
    - Published guidance describes conditions, restrictions, etc.
    - Transaction must meet all of the conditions to qualify for exemption
    - PPA added specific exemptions for certain investment advice arrangements