Collective Investment Trusts
Lower Costs and Greater Flexibility

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As defined contribution (DC) plans continue to grow as a source of retirement savings, many plan sponsors are looking to bring best practices from the defined benefit world into their DC plans. We believe the increasing popularity of collective investment trusts (CITs) among plan sponsors reflects the trend toward a more institutional approach to investing in DC plans. A recent study published by Callan Associates shows that some 65% of surveyed DC plans offered at least one CIT in 2017, up from 44% in 2011.[1] In addition to providing the potential for lower overall costs, CITs may offer plan sponsors more options for accessing institutional quality investment strategies while maintaining ERISA fiduciary standards.

Although traditionally offered by primarily the largest plan sponsors, CITs are now being considered by smaller plan sponsors for a number of reasons, including an increasing focus on plan expenses, pricing flexibility and availability on distribution platforms. Looking ahead, we expect CITs to continue capturing a growing share of defined contribution plan assets from plans of all sizes. CITs and mutual funds typically serve a similar function within a defined contribution plan. Both can provide participants with high-quality, professionally managed investments that, in most cases, offer daily valuation and liquidity. Additionally, both may offer a variety of pricing structures to suit different market segments.

While CITs and mutual funds are similar, there are still some key differences to keep in mind, including how they are regulated, their cost structures and the degree of flexibility that each may offer plan sponsors. We'll briefly examine some of those differences here.

The Basics — What is a CIT?

Many CITs, like mutual funds, are pooled investment vehicles managed collectively in accordance with a common investment strategy. While mutual funds are typically maintained by an asset management company and available to most retirement plans and retail investors, many CITs are maintained by a bank or trust company and only offered to certain qualified retirement plans. In addition, CITs have a separate set of regulators from mutual funds and typically are restricted from making fund information available to the general public. Nonetheless, in many cases, participants can find information online about their CITs by using designated web portals, often established by their recordkeeper or plan sponsor.

Regulatory Structure of CITs

A key difference between CITs and mutual funds is how each vehicle is regulated. Mutual funds are regulated by the Securities and Exchange Commission (SEC), among other statutes, under the Investment Company Act of 1940, as amended. Their governing documents primarily consist of a prospectus and statement of additional information. While mutual funds are typically available to both retail and institutional investors, CITs are generally only available to certain qualified retirement plans and do not have publicly available fund information and tickers. CIT providers are often regulated by the Office of the Comptroller of Currency (OCC), as well as the IRS and DOL, and CITs may be governed by a declaration of trust and investment/operating guidelines. Many CIT managers also have an additional layer of oversight in that they are held to ERISA fiduciary standards. This means that they must manage plan accounts solely in the interest of such plan's participants and beneficiaries.

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Figure 1: At a Glance

Characteristics	CITS	Mutual Funds
What Are They?	Commingled investment vehicles typically maintained by a bank or trust company and only offered to certain qualified retirement plans	Commingled investment vehicles typically maintained by an asset management company and available to most retirement plans as well as the general public
Oversight and Regulation	Often regulated by Office of the Comptroller of Currency (OCC) and the IRS and DOL Fund Trustee can be subject to ERISA standards aimed at protecting plan participants	Regulated by the Securities and Exchange Commission (SEC), among other statutes, under the Investment Company Act of 1940 as amended Manager not held to ERISA standards
Governing Documents	May be governed by a Declaration of Trust and investment/operating guidelines For participants, usually provide fund fact sheets or work with third party provider to create them	Primarily a prospectus and Statement of Additional Information For participants, usually provide fund fact sheets or work with third party provider to create them
Reporting	Audited Financial Statements Subject to DOL and ERISA reporting requirements, including but not limited to Form 5500 Schedule C and Sections 404a-5 and 408(b)(2) of ERISA	Annual Report Subject to DOL and ERISA reporting requirements, including but not limited to Form 5500 Schedule C and Sections 404a-5 and 408(b)(2) of ERISA
Fee Structure	May have multiple share classes Potential for negotiated pricing arrangements	May have multiple share classes
Trading	Most can trade via NSCC Usually daily valuation	NSCC trading Usually daily valuation

Lower Costs and Increased Flexibility

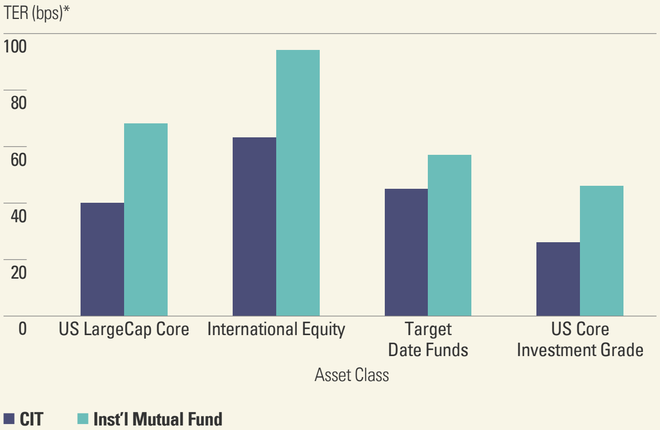
Amid increased public attention to DC plan expenses, many plan sponsors are looking for lower cost solutions. CITs typically have lower expenses than mutual funds because in many cases they have lower marketing costs, no board of directors, no SEC filing requirements and generally have lower overhead. CITs may also offer more flexibility in pricing, allowing for customized arrangements based on overall plan size. As plan-level assets within a CIT increase, for example, fees could potentially decrease. Additionally, the share class creation process can be quicker for CITs. There are other structural advantages to CITs that can help to lower costs. One way is through their ability to take advantage of certain internal cross trading practices, which lowers the transaction and trading costs incurred by the fund. CITs also benefit from certain tax advantages, especially with international investments, given their mainly institutional and retirement plan investor base. In total, lower fund costs can potentially provide increased retirement savings to participants.

How CITs Keep Costs Low

- Can have lower overhead
- Typically exempt from SEC registration and ongoing SEC requirements
- Lower potential trading costs through cross-trading securities among a manager’s investment strategies
- Lower retail marketing expenses
- Potential advantageous tax treatment for international funds due to qualified investor base
- Ability of some CIT providers to offer customized pricing arrangements based on plan size

Figure 2: Comparing Expense Ratios for CITs vs. Mutual Funds

CITs may offer a cost advantage over mutual funds



Source: Mercer Global Asset Manager Fee Survey 2016.
* Fees assume $100M asset minimum level.

An Institutional Approach to Investing

Retail mutual fund managers typically manage portfolios with the needs of both taxable and tax-exempt investors in mind. In contrast, many CITs designed for retirement plans are managed exclusively to meet the needs of tax-exempt investors, making them an attractive choice for many plan sponsors. With an institutional focus, CITs can offer DC plan participants the type of high-quality, low-cost investment strategies enjoyed by pension funds and other institutional investors. Furthermore, CITs can provide sponsors access to more alternative investment strategies that may not be available in a mutual fund. Finally, as institutional investment vehicles, many CITs allow for white labeling by plan sponsors. This can create more flexibility for plan sponsors in designing and naming their investment menu. For example, a plan sponsor could combine multiple managers into a single investment option for participants, such as "the ABC Company Large Cap Equity Fund." Customizing the name of investment strategies can help participants better understand the products in which they are investing.

Figure 3: Retirement Plans Eligible to Use CITs

Typically Eligible	Typically Not Eligible
Qualified 401(k) plans	403(b) plans
Qualified profit sharing plans	457(f) plans
Qualified stock bonus plans	IRAs and Keoghs
Qualified pension plans	Endowment plans
401(a) government plans	Foundation plans
457(b) government plans	
Certain separate accounts and contracts of insurance companies	

Communicating CIT Information to Participants

Today, most CITs are valued daily, can offer transparency of holdings and are traded via the National Securities Clearing Corporation (NSCC). In addition, most CIT managers will provide plan sponsors with participant fact sheets or will help develop them working with a third party. Such fact sheets can help participants understand certain key holdings and sector exposures of a CIT's investment strategy.

Many providers, including State Street Global Advisors (SSGA), also allow for their CIT information to be made available on data and fiduciary platforms such as Morningstar®, making it easier than ever to pull information on CIT options.

Keep in mind that CITs are not regulated by the SEC, so participants will not be able to access their daily fund information or research a ticker symbol through public web sites or news sources. However, participants may be able to access daily fund information through their plan's designated online portals. When adopting CITs, plan sponsors will likely need to educate participants about where and how to access fund information online.

Growth on Recordkeeping Platforms

A growing number of recordkeepers are now able to support robust reporting services for CITs. Plans of all sizes can now access certain CITs through most recordkeeping platforms. If operational changes are necessary, many CIT providers are willing to work with recordkeepers to accommodate reporting requirements. If you're a plan sponsor who is considering CITs, we suggest having an in-depth conversation with your recordkeeper about their capabilities, available investment options and any changes to your service that may be associated with adding CITs to your investment options. Your recordkeeper's experience and expertise can be a valuable resource when introducing CITs to your plan.

Exploring Your Options

The choice of using CITs, mutual funds or both in your plan will likely depend largely on the size of your plan, the type of plan you offer and your objectives as a plan sponsor. We believe the current CIT market provides a diverse selection of assets classes as well as differentiated share classes for plan sponsors. From an operational and transparency perspective, CITs have evolved to accommodate the needs of defined contribution plans.

Here are some possible conversation starters for your DC plan's investment committee as you consider various types of investment vehicles:

- How can you best serve the investment needs of your participants?
- What impact would lower fees have on your participant's long-term investment success?
- What types of investment vehicles can your current recordkeeper support?

[1] Source: Callan 2018 Defined Contribution Trends Survey.

Learn More

At SSGA, we invite you to begin a conversation about exploring the types of investment vehicles that might make the most sense for your plan.

To learn more about our funds, please email us at DCIntermediaryTeam@ssga.com.

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