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OPINION

CITs Need Boards? 401(k)s Sure Don't Think So

Though the trusts' governance structure differs from mutual funds', they hew to no less rigorous oversight standards; corporate retirement plans wouldn't use them otherwise.

By Jason Levy | February 4, 2025

The House of Representatives, Senate and retirement experts including Boston College's Center for Retirement Research agree: 403(b) retirement plans should have access to collective investment trusts because they are strictly regulated, transparent and often confer meaningful cost savings and increased protections to retirement investors.

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Secure 2.0 Act amended the Internal Revenue Code to allow 403(b)s in CITs, and legislation passed in the House last year and likely to be reintroduced this year with bipartisan support would finish the job of providing this access.

The widespread support for those bills has focused attention on the retirement security enhancements that will be available to participants in 403(b)s when they receive the same access to CITs afforded to private sector retirement plans like 401(k)s for decades.

Ignoring these considerable benefits, the president of Versanture Consulting argued in a commentary in December that 403(b)s should not have equal access to CITs based on false premises that CITs are subject to "reduced oversight" to which independent directors "are key," in addition to being less transparent and providing fewer protections.

These claims couldn't be further from the truth.

CITs are, in fact, subject to strict regulatory oversight and robust governance. The stringent regulatory structure imposed on them yields two distinct layers of oversight tailored to protect retirement investors, neither of which is dependent on board oversight.

First, whereas mutual funds are governed by boards of directors that are required to include independent directors, CITs are governed by trustees that must adhere to a regulatory regime founded on fiduciary principles arising under state or federal banking law, common law and, critically, the Employee Retirement Income Security Act. These overlapping fiduciary obligations mandate that the CIT trustee, among other things, follow prudent investment practices, exercise investment oversight, and manage the investment fund with undivided loyalty for the financial benefit of participants and beneficiaries who are invested in the fund.

Second, independent from the CIT trustee, the responsible decisionmaker who selected the CIT as an investment in an employer-sponsored plan has the same fiduciary obligations in selecting and overseeing the CIT investment.

The Versanture article is wrong to state that this second group of employer plan fiduciaries is "solely" responsible for CIT oversight. While employer plan fiduciaries provide a second layer of oversight, it is the CIT trustee who has day-to-day fiduciary obligations to manage the fund.

Given the weight of the CIT trustee's legal obligations, there is no basis to argue that such trustees possess any less of the skillset and expertise as outside directors to mutual funds, nor is there any other basis to conclude that a mutual fund governance model that utilizes a board of directors is the exclusive means to afford protection to retirement plan investors.

Erisa coverage of CITs helps illustrate why. Because they can be offered only to retirement plans, virtually all CITs accept investments from plans that are subject to Erisa – a critical feature ignored by the Versanture article. If an Erisa plan invests in a CIT, the CIT, its trustee and its investment manager are subject to the law's full array of fiduciary duties, described by appellate courts as "the highest known to the law."

They are also required to comply with Erisa's strict "prohibited transaction" rules and must make fulsome disclosures concerning the fees and other amounts charged to benefit plan investors or otherwise received by them.

By contrast, the assets of a mutual fund are not considered Erisa plan assets and therefore the manager of a mutual fund in which a plan invests is not subject to Erisa's fiduciary obligations.

In addition to Erisa protections, CITs and their trustees are also subject to regulation by federal or state bank regulators as well as to fiduciary duties under common law. Though

CITs are not subject to registration under the '40 Act or Securities Act of 1933, they remain securities for purposes of the anti-fraud provisions under the Securities Act of 1934.

Given the robust regulation of CITs, it is patently false to argue that they are subject to "reduced oversight" or offer "reduc[ed] protections for 403(b)s" merely because they are structured differently from mutual funds and do not have boards of directors.

Rather than being less regulated and transparent, CITs' most marked contrasts from mutual funds are their typically lower cost – and, for now, their exclusion from 403(b)s. Ending that exclusion and giving 403(b) participants access to lower-cost investments is a win-win.

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