FINANCIAL CONCEPTS INC
A MEMBER FIRM OF M FINANCIAL GROUP
Executive Compensation ■ Succession ■ Wealth Transfer Planning

M Financial Group™

Q1 2021

QUALIFIED PLAN NEWS

CAPITAL MARKETS REVIEW					PERIOD ENDING MARCH 31, 2021	
Index	Qtr	Ytd	1 Yr Return	3 Yr Return	5 Yr Return	10 Yr Return
S&P 500 TR USD	6.17	6.17	56.35	16.78	16.29	13.91
Russell 2000 TR USD	12.70	12.70	94.85	14.76	16.35	11.68
Russell 3000 Value TR USD	11.89	11.89	58.38	10.99	11.87	10.91
Russell 3000 Growth TR USD	1.19	1.19	64.31	22.39	20.87	16.35
MSCI ACWI Ex USA NR USD	3.49	3.49	49.41	6.51	9.76	4.93
BBgBarc US Agg Bond TR USD	−3.37	−3.37	0.71	4.65	3.10	3.44
FTSE Treasury Bill 3 Mon USD	0.02	0.02	0.21	1.45	1.15	0.60

MARKET COMMENTARY

The U.S. equity market advanced 6.3% during the quarter. Progress in the distribution of COVID-19 vaccines supported U.S. equities in the period, as the prospects of the economy fully reopening boosted investor confidence. The passage of a third stimulus bill further aided U.S. stocks in the period, despite some concern of rising inflation.

Value stocks outperformed growth stocks for the second consecutive quarter. The continued rebound was due to increases in interest rates, commodity prices, and continued optimism for more economically sensitive companies, which are primarily in value-oriented sectors.

Small-cap stocks outperformed both the mid- and large-cap segments of the market in the quarter. All capitalization segments of the market posted strong returns in the one-year period, with small-cap stocks outperforming mid- and large-cap stocks by 21.2 and 38.4 percentage points, respectively.

The energy and financial sectors posted the strongest returns for the second consecutive quarter. The technology sector had the weakest return in the quarter, as higher interest rates typically impact higher-growth companies more negatively than companies with lower growth expectations.

Foreign stocks returned 3.5% in the quarter as declining COVID-19 infection rates and expanding distribution of COVID-19 vaccines supported expectations for greater global economic growth. Continued fiscal and monetary support from governments and central banks also contributed to strong returns.

The U.S. dollar appreciated by over 2% against most major currencies during the quarter, detracting from returns of foreign stocks for U.S.-based investors. Value stocks outperformed growth stocks in the quarter. Continental Europe returned 3.5% in the quarter, despite lower vaccination rates relative to the U.S. and U.K. due to availability and safety concerns.

Japan's 1.6% return in the quarter trailed other developed market equity returns, largely due to the negative impact from currency. Emerging-markets equities increased 2.3% in the quarter. A pickup in global economic activity and rising commodity prices generally aided emerging-markets performance, while a stronger U.S. dollar and slow vaccination rollouts negatively impacted emerging markets during the quarter.

Preliminary estimates from a subset of core real estate managers indicate a positive return for the quarter. Over the last year, industrial and multifamily properties have performed better than holdings within the office and retail segments of the market.

The U.S. fixed income market declined 3.4% in the quarter. Interest rates rose during the quarter as investors anticipated higher levels of economic growth associated with the U.S. economy reopening. Additional government borrowing for stimulus packages and a potential increase in inflation also added upward pressure on interest rates.

The 10-year Treasury yield increased from 0.93% to 1.74% during the quarter. These interest rate pressures resulted in U.S. government bonds declining 4.1% and U.S. investment grade bonds declining 4.5% for the quarter.

Non-investment grade corporate bonds rose 0.8% on the prospect for better economic conditions. Developed non-U.S. government bonds declined 2.4% in the quarter, but U.S.-based investors experienced a -6.4% return due to a stronger dollar.

Treasury inflation protected securities (TIPS) decreased 1.5%, which outperformed conventional Treasuries in the quarter as inflation expectations increased. The breakeven inflation rate implied in 10-year U.S. TIPS ended the quarter at 2.37%, versus 1.99% at the end of the prior quarter. The realized annual CPI was 1.6% through February 2021.

DEPOSITING PLAN CONTRIBUTIONS

As a plan sponsor, you know how important it is to comply with the many government regulations that affect your plan. One area that has caused confusion among plan sponsors is the deadline for depositing employee contributions into the plan's trust account.

General rule. Federal pension regulations provide that employee contributions become plan assets as of the earliest date on which the contributions can reasonably be segregated from the employer's general assets. Since this earliest date rule does not set a clear-cut deadline, employers have had to make their own determination of what is reasonable and hope that it won't be challenged if government auditors examine the plan.

Cost of noncompliance. Not getting it right can prove costly. Failure to deposit contributions timely is considered a prohibited transaction and may result in significant penalties, including possible loss of the plan's tax-qualified status.

Seven-day safe harbor. Employers that sponsor small plans (those with fewer than 100 participants) can avoid potential problems by satisfying a seven-day safe harbor rule. Under the safe harbor provision, employers that deposit employee contributions in a plan account within seven business days after the contributions are withheld from employees' wages or received by the employer will automatically satisfy the law's requirements. Allocations to specific participant accounts and investments do not have to be completed within the seven-day window as long as the contributions have been deposited in the plan. A similar seven-day safe harbor is available for deposits of plan loan repayments.

Note that sponsors of large plans — 100 participants or more — must continue to deposit contributions as of the earliest date the contributions can reasonably be segregated from the employer's general assets.

CHECK FIDUCIARY LIABILITY COVERAGE

Pension law (ERISA) generally requires that every fiduciary of an employee benefit plan and any other person who handles plan money be covered by a fidelity bond. The fidelity bond protects the retirement plan against misappropriation of funds by individuals handling the plan's assets. However, the fidelity bond does not protect against claims for losses sustained because of a breach of fiduciary duty.

Fiduciary Liability Insurance Protection

Fiduciary liability insurance provides protection for trustees and other plan fiduciaries in the event of a breach of fiduciary duty. These policies typically cover settlements or judgments. Wrongful acts that may be covered by fiduciary liability insurance include:

- Negligent investment practices
- Failure to diversify investments
- Failure to file required reports
- Conflicts of interest
- Errors in computing eligibility
- Inadequate instructions to beneficiaries that cause a loss of benefits

The benefit plan itself can purchase fiduciary liability insurance. However, the policy must allow the insurer to seek recourse against the fiduciary if it is determined that the fiduciary breached his or her duty to the plan. Commonly, the employer purchases the insurance as part of the overall compensation package of company executives who assume responsibility over the company's benefit plan.

Check Coverage Carefully

Fiduciary liability insurance coverage varies widely from policy to policy, so it's important to check what is covered in your policy and determine if you need additional coverage.

Occurrence or claims-made policies. Most policies are claims-made policies that only cover claims made and reported during the policy period. Look to obtain an occurrence-basis policy that covers all acts that occurred during the policy period, no matter when claims are made.

Aggregation of wrongful acts. If "wrongful act" is defined vaguely in a policy, insist upon a clear, objective definition. A wrongful act is generally defined as a breach of duty under ERISA, another federal law, or state law. If multiple wrongful acts may be treated as part of an interrelated series of wrongful acts, negotiate the elimination of this provision. Otherwise, this aggregation provision may allow the insurer to allocate a new claim as part of a prior claim, which may limit what is paid on the claim (if the policy's annual limit is unavailable to pay the claim).

Nonrecourse riders. If the policy is purchased with plan assets, the policy must allow the insurer to recover any paid losses from the fiduciary whose breach caused the loss. To protect themselves, individual fiduciaries can purchase nonrecourse riders. Under a nonrecourse rider, the insurer waives its subrogation rights against the fiduciaries in cases that do not involve fraud, willful neglect, or criminal wrongdoing.

Defense costs. To help ensure adequate defense coverage, fiduciaries may want to purchase a separate defense policy, since many policies count any costs of defending an action against the overall policy limit. Also, a policy may require you to accept defense counsel appointed by the insurer. Purchasing a separate defense policy will allow you to name your own defense counsel.

Punitive damages or fines. Since most policies will not pay punitive damages, you may want to negotiate coverage of punitive damages. Even if a policy covers the 20% penalty tax on fiduciary violations, it may not cover the 15% initial excise tax on prohibited transactions.

WEB RESOURCES FOR PLAN SPONSORS

Internal Revenue Service, Employee Plans
› irs.gov/ep

Department of Labor, Employee Benefits Security Administration
› dol.gov/ebsa

401(k) Help Center
› 401khelpcenter.com

BenefitsLink
› benefitslink.com

Plan Sponsor
› plansponsor.com

Plan Sponsor Council of America
› psca.org

Employee Benefit Research Institute
› ebri.org

S&P 500 is a commonly used measure of common stock performance. Russell 2000 is a commonly used measure of small capitalization stocks. Russell 3000 Value measures performance of U.S. equity universe broad value segment with lower price-to-book ratios and lower forecasted growth values. Russell 3000 Growth measures performance of Russell 3000 Index companies with higher price-to-book ratios and higher forecasted growth values. MSCI ACWI EX U.S. tracks 850 stocks traded in 22 world markets (excludes U.S. based stocks). Barclays U.S. Aggregate Bond Index tracks domestic investment grade bonds (including corporate, government, and mortgage-backed securities). Citigroup 3-Month U.S. Treasury Bill Index tracks short-term U.S. government debt instruments. All referenced indices are unmanaged and not available for direct investment. Past performance is not a guarantee of future results.

To learn more, please contact:

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