CIT Myths and Facts

Collective investment trusts (CITs), also referred to as commingled trusts or collective trust funds, are pooled investment funds that are administered by banks and trust companies and are designed exclusively for qualified retirement plans. These often misunderstood funds are becoming as easy to use as mutual funds and may be a valuable tool in developing a retirement plan lineup—that is, once the facts are distinguished from the myths. Below are several common myths about CITs, along with the related factual information.

Structure, Documentation and Accessibility

Myth: **CITs are exactly like mutual funds.**

Fact: CITs are similar to mutual funds, but there are a few important differences. Generally speaking, CITs tend to be more cost-effective and may offer flexible pricing. CITs typically have lower administration and marketing and distribution costs when compared with mutual funds.[1]

Myth: **CITs have a lower level of regulatory oversight than mutual funds.**

Fact: While CITs are exempt from registration with the Securities and Exchange Commission (SEC) these funds are subject to a variety of federal and state laws and regulations. To the extent ERISA plan assets are invested, CITs are subject to ERISA and U.S. Department of Labor (DOL) regulations. CITs must comply with certain Internal Revenue Service rules in order to maintain their "group trust" tax-exempt status. CITs must be sponsored and maintained by a bank or trust company; depending upon the charter (national or state) of the CIT provider, the primary regulator of the bank or trust company and the CITs will be the Office of the Comptroller of the Currency (OCC) or the state banking examiner. To the extent a CIT is marketed by a broker-dealer, the broker-dealer must comply with Financial Industry Regulatory Authority (FINRA) rules relating to sales of exempt securities. In addition, if a CIT invests in commodity interests, the CIT provider (or sub-adviser) will have to comply with the rules and regulations of the Commodity Futures Trading Commission (CFTC). CITs are also audited annually by independent auditors.

[1] Cerulli's Institutional Markets 2013

Myth: **CITs don't have any documents like a mutual fund prospectus, so the investor cannot make an informed decision.**

Fact: CITs are not registered with the SEC and therefore, unlike mutual funds, are not required to prepare prospectuses. A CIT is established and governed by its Declaration of Trust, which sets forth the fund's terms and conditions (e.g., investor eligibility, valuations, subscriptions and redemptions). Most CIT providers also prepare a fund offering document, which may be called a Fund Disclosure, Fund Description or Statement of Characteristics that further describes, among other things, the fund's material terms, investment objective and strategy, policies, fees/expenses and risk characteristics. These documents are designed to provide similar information to that which an investor would find in a mutual fund prospectus.

Myth: **CITs are not broadly available on recordkeeping platforms, making it difficult to add a CIT to a plan's investment lineup.**

Fact: Most CITs are now traded on Fund/SERV®, the industry standard for processing and settling mutual fund transactions offered by the National Securities Clearing Corporation (NSCC), making them easy for recordkeepers to include on their platform alongside mutual funds. Many recordkeeping platforms have multiple CITs available, so a plan sponsor has the flexibility to offer the best possible vehicle for plan participants.

Myth: **CITs have high account minimums, making them only available to large plan sponsors.**

Fact: Some CITs may have a higher minimum investment amount than a typical mutual fund, but other CITs have very small minimum investment amounts (especially if traded through Fund/SERV®). For those CITs that do have higher minimums, recordkeepers may offer omnibus structures, making it possible for small and medium-sized plans to access CITs with few or no minimum investment requirements.

Myth: **Very few plans are eligible to use CITs.**

Fact: Many types of retirement plans can invest in CITs, including plan types such as 401(k), profit-sharing, pension, stock bonus, thrift, money-purchase, governmental retirement, cash balance and certain Puerto Rico retirement plans. Under certain circumstances, CITs may accept investments from church plans.

Myth: **CITs aren't always daily traded, so they're not appropriate for DC plans.**

Fact: Historically, this may have been true. Today, the vast majority of CIT providers offer daily traded, daily priced funds.

Myth: CITs offer a limited selection of asset classes.

Fact: CITs are now available in a wide variety of asset classes, both passively and actively managed, including domestic equity, international equity, fixed income, stable value and alternatives. Additionally, CITs have become popular in glide path/target-date funds (TDFs).

Myth: Large plans prefer separate accounts.

Fact: Many large plans prefer CITs over separate accounts to escape the added administration necessary to maintain a separate account. Separate accounts may also incur additional legal costs associated with the review and negotiation of required documents, such as ISDA master agreements, sub-custodian and futures agreements.

Fees

Myth: CITs are more expensive than mutual funds.

Fact: On average, CIT fees can be 25 to 40 basis points less than mutual fund fees.[2] CITs typically have lower administration and marketing and distribution costs as compared with mutual funds. These features often result in cost savings for the CIT which are then passed on to plan sponsors and participants.

Myth: Many plans require fee flexibility, such as revenue sharing, which is only available in mutual funds.

Fact: Many CIT providers now offer a variety of fee structures that are included in the net asset value (NAV) of each share: zero revenue sharing, a certain amount of revenue sharing or custom revenue sharing, allowing plan sponsors to customize the payment of fees based on the specific needs of their plan. Additionally, a plan may negotiate management fees on certain types of share classes.

Myth: Fees for CITs aren't as transparent as mutual funds.

Fact: With the release of the DOL mandatory disclosure requirements for retirement plan sponsors under ERISA section 408(b)(2), CIT providers prepare all necessary disclosures regarding the services being performed, as well as compensation (both direct and indirect). A CIT provider should also furnish recordkeepers with the disclosure information needed to communicate to participants as required under ERISA section 404(a)(5), in addition to quarterly reports detailing fees and expenses.

[2] Ignites: CITs: A Cheaper Option Many Sponsors Ignore, July 1, 2013

Data Availability and Reporting

Myth: CITs don't have the same level of reporting as mutual funds.

Fact: While reporting can vary by provider, most leading CIT providers offer similar reporting to mutual funds, including: daily prices, monthly net and gross performance, monthly and/or quarterly holdings, and fact sheets.

Myth: Third-party data providers, such as Morningstar, don't have the information needed to monitor or analyze CITs.

Fact: Many providers, including Morningstar, offer specific CIT databases available under licensing agreements. Since 2006, Morningstar has increased the number of CITs it tracks by 55%. Plan consultants are also creating and maintaining robust databases to enable fiduciaries to monitor and analyze CITs. While the data support structure for CITs is not yet at the level of mutual funds, the gap continues to close.