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**Investments**

**Trust Employee  
Benefits Outsourcing:  
FASTER, BETTER,  
STRONGER**



**F**OR MOST BANKING INSTITUTIONS, the question is not whether they should outsource high-cost, low-value retirement plan recordkeeping operations, but when. Banks should review their trust operations as they relate to employee benefits services and consider outsourcing as a way to grow their retirement plan business, reduce overall costs of service delivery, and increase client satisfaction. After the decision to outsource has been made, identifying the right outsourcer can be the difference between working with a vendor and having a true partner. Matching bank challenges with vendor deliverables is key to finding the right partner.

Banks large and small are being scrutinized by their stakeholders as allegations of failures, bailouts, and mismanagement scream from the news headlines.

Bank executives are on the hook to contain costs, create value, and serve their client markets in the most efficient manner possible. Even well-managed, sufficiently capitalized institutions feel the pressure to review divisional operations to ensure that profitability is being maximized at all levels.

One significant strategy deployed by banks for containing costs while increasing efficiencies is outsourcing. Common bank operations that have been successfully outsourced include check clearing, student loan processing, and mortgage servicing.

A review, then, of a trust division's employee benefits and retirement plan operations should be part of a bank's overall strategic business review and planning. The top-of-mind consideration for this review: Is there a need or an opportunity for outsourcing?

Retirement plan recordkeeping, administration, and custody outsourcing is becoming increasingly important for bank trust departments as internal pressures and external market demands increase. From an intra-bank perspective, all banking divisions are being asked to

- increase revenue contributions
- reduce overhead expense
- streamline operations
- mitigate risk
- meet audit demands
- comply with legislative and regulatory requirements

At the same time, the retirement plan sponsor looks to the trust division for:

- fiduciary support services
- state-of-the-art account access services, including Web, voice, and call center
- full fee disclosure
- employee communication, education, and enrollment services
- burden-free administration that is automated, accurate, and timely
- unwavering personal relationship management

Delivery of retirement plan services through trust organizations is further complicated by the significant security risks (e.g., identity theft) presented by the electronic age.

## The Challenge

In the fast-changing retirement plan environment, bank executives must address the following development areas, questioning whether retaining internal operations is in the best interest of stakeholders and the best use of resources or whether outsourcing is a viable strategic consideration. The cost-value proposition has shifted and banks must adjust service delivery models accordingly.

### 1. Profitability

There is significant cost to the delivery of a retirement plan product to the market. Because that market is heavily regulated and constantly changing, it can be hard to justify the expense of supporting small books of plans, i.e., fewer than 300. Consider the following general cost categories:

**Systems/technology.** The challenge for most banking institutions relevant to participant-level recordkeeping, whether vendor licensed or legacy system, is the constant evolution inherent with technology that requires evaluation, acquisition, programming, enhancement, and maintenance. With insufficient business scale, the technology cost per plan or participant can greatly reduce profit margins.

Utilizing bank technology staff to support an ancillary, non-core banking system can create a drag on bank technology resources.

**Personnel.** Retirement plan administration requires technical specialists who are well versed in retirement plan fundamentals. Industry monitoring, professional education, and functional training are key components. Finding a pool of qualified professionals from within the bank footprint and then keeping those professionals current with IRS and Department of Labor legislative and regulatory changes can be a significant challenge.

### 2. Risk

**Financial.** Bank standards and audit controls can mitigate risk, but the internal control structure and relevant policies and procedures must be sufficiently adequate, monitored, and tested to ensure operational integrity and limit liability.

From contribution and investment trade processing to distribution and loan administration, the management of the retirement plan has the potential for error and, ultimately, financial liability and loss.

**Data security.** Gramm-Leach-Bliley Act (GLBA), the Bank Secrecy Act, Sarbanes-Oxley, the Federal Financial Institutions Examination Council (FFIEC)—each of these regulations places a heavy burden on the bank for the safety and protection of the customer from identity theft. The cost to protect data only continues to rise in an economy where technology is the constant driver.

**Reputation.** Plan administrative errors, processing missteps, breaches of data security—any one of these has the potential to irreparably damage a bank's reputation as a trusted financial partner and leader.

### 3. Growth and Brand Protection

When banks focus on the “how” of doing business and not the “who,” opportunities are lost. Business development stagnates when a trust division must focus on and invest personnel resources in the day-to-day administration needs of their retirement plan clients. For example, as baby boomers move toward retirement, a gold mine of cross-selling opportunities exists for any organization that is properly positioned within the employee benefit marketplace.

A bank's brand is the sum of its differentiating factors. From visible branding (colors and logos) to experience branding (customer interactions and perceptions), placing the focus on core competencies (fiduciary and investment services) and the resulting value propositions will support protection of the bank's brand and achieve greater financial gains.

### Challenge Summary

Thoroughly review

- operations and systems
- core competencies
- depth of expertise within the division
- expense management
- size of market

A thorough review of your current situation will illustrate that there is little to no value added by having the banking institution involved in running the internal recordkeeping engine. Viewing the retirement plan business as a potential profit center can support long-term strategic interests and business opportunities and lead to discussions of outsourcing.

### The Option

Outsourcing as a means to reduce costs, mitigate risk, create scalability, and obtain specialized skills is not new to the banking industry. But while it is not foreign, the scope of employee benefits and retirement plan services outsourcing has been limited. Divisional heads can be hesitant to let go of the internal administrative reins, so outsourcing of the following independent services is more likely than that of recordkeeping:

- plan documents
- plan-level administration, compliance, and accounting services
- custody and paying agency services
- trading settlement
- participant enrollment/communication

Fully bundled solutions that deliver all of the above, wrapped around a core recordkeeping technology, are often overlooked as a viable alternative.

### The Solution

To further productivity and achieve profitability gains, banking executives are encouraged to recommend and support initiatives to move to a recordkeeping outsourcing solution for their trust retirement plan services. By outsourcing recordkeeping and trade functions, banks can move hard-dollar costs off the

books and reduce operating expenses. Outsourcing allows trust to re-focus efforts on enhancing existing client relationships and generating new sales growth.

At a glance, the benefits of outsourcing include:

- removing trust department daily trade liability, which can be significant
- eliminating hard-dollar costs related to day to day operational functions on income statement
- eliminating “technology” enhancement maintenance
- eliminating the staff and regulatory costs of complying with FFIEC for a non-core banking system
- eliminating expenses associated with recordkeeping systems and technology upgrades
- providing opportunity for redeployment of human resources

Two alternative outsourcing solutions are illustrated (see Figure 1).

### The Selection

Careful examination of the retirement plan outsource provider market (which is vast) for a solution that has a specific bank focus and can meet each of the challenges identified above should be employed. Here’s a brief examination of each provider requirement.

#### 1. Profitability

**Technology.** Purchasing, maintaining, and upgrading both hardware and software systems used to keep records for and administer retirement plans carry considerable costs in terms of capital and human resources. When considering a recordkeeping outsource partner, banks will want to weigh heavily the value of the provider in terms of:

- system used
- ownership
- maintenance services for the product, enhancements, updates, program corrections, and other service practices
- scalability of the system
- connectivity with trust systems for plan-level accounting

Beyond the recordkeeping and administration, other technologies (e.g., mutual fund trading, Web, voice response, and compliance interfaces) must be fully integrated and service-oriented. Examples of required technology connections include:

- trust interface
- daily reconciliation files
- toll-free interactive voice response system (VRS)
- transactional Internet access for participants
- Internet access for plan and participant information reporting for plan sponsors

**Personnel.** To successfully administer today’s 401(k) plans, vendor administrative staff must have a high degree of knowledge and expertise and must receive continuous

education and training, preferably via an accredited industry program. Preferred outsourcing vendors are those whose employees carry professional and industry credentials such as the following:

- Certified Employee Benefit Specialist (CEBS)
- Certified Retirement Services Professional (CRSP)
- Certified Public Accountant (CPA)
- Accredited Investment Fiduciary Analyst (AIFA)
- Chartered Financial Consultant (ChFC)
- Qualified 401(k) Administrator (QKA)
- Qualified Pension Administrator (QPA)
- Certified Pension Consultant (CPC)

Figure 1: Two alternative outsourcing solutions	
Partial Outsource (Self-Custody) Model	Total Outsource Model
Functions Outsourced	Functions Outsourced
<ul style="list-style-type: none"> <li>• Participant accounting &amp; reporting</li> <li>• Web/VRU client interface</li> <li>• Call center interface</li> <li>• Compliance</li> <li>• Documents &amp; 5500 preparation</li> <li>• Loan &amp; distribution calculations</li> <li>• Trade execution</li> <li>• Payroll processing</li> </ul>	<ul style="list-style-type: none"> <li>• Participant accounting &amp; reporting</li> <li>• Web/VRU client interface</li> <li>• Call center interface</li> <li>• Compliance</li> <li>• Documents &amp; 5500 preparation</li> <li>• Loan &amp; distribution calculations</li> <li>• Trade execution</li> <li>• Payroll processing</li> <li>• Plan-level custody</li> <li>• Contribution processing</li> <li>• Checks and 1099-R preparation</li> </ul>
What Remains?	What Remains?
<ul style="list-style-type: none"> <li>• Plan-level custody</li> <li>• Contribution processing</li> <li>• Checks and 1099-R preparation</li> <li>• Client relationship management</li> <li>• New business development</li> <li>• Investment oversight</li> <li>• Employee education</li> </ul>	<ul style="list-style-type: none"> <li>• Client relationship management</li> <li>• New business development</li> <li>• Investment oversight</li> <li>• Employee education</li> </ul>

- Qualified Plan Financial Consultant (QPFC)

Further, every vendor should have a ready resource of trained, specialized professionals, including recordkeeping and technology staff, for hire within their geographies.

#### 2. Risk

**Bank audit structure.** Banks must partner with outsourceurs that understand bank and regulatory auditing practices and have the appropriate security, policies, and procedures in place to protect client data. A potential vendor must maintain a comprehensive audit structure, including but not limited to the following:

- SEC audit as transfer agent (at least once every five years)
- general controls and network security assessments
- internal and external penetration assessments
- SAS-70 Type-II covering 12 months (annual)

Consider that when bank auditors review your vendor due diligence, you must be confident that it will hold up to their scrutiny.

**Data protection.** The retirement plan outsource vendor should have a thorough knowledge of:

- the GLBA and its policy requirements for the protection of information from threats to security and data integrity
- FFIEC guidelines recognizing and adhering to the guidance on information security

The vendor must be committed to the protection of hardware, software, communication networks, and data and adhere to the following or similar practices:

- Maintain audited controls that provide assurance that physical access to data processing facilities is restricted to those with proper authorization.
- Have a state-of-the-art firewall, intrusion prevention system, and VeriSign SSL 40/128 bit encryption to safeguard the personal identifiable information on the Web site.
- For participant security, have PC multiple authentication and visual cue programs to protect user and PC integrity and offer user-selected usernames and passwords (PINs) to access all associated account-related information.
- Maintain its own outside vendor due diligence program to ensure that each of its vendors performs all levels of data encryption and protection to current regulation guidelines and conducts an annual review of these vendors and their associated systems and infrastructure to ensure compliance.
- Provide data intrusion prevention protection including server performance and application monitoring, and an enterprise-wide antivirus system. At least once per year, have an independent firm conduct penetration testing to determine that the network is secure from both internal and external threats.
- Utilize a climate-controlled, secure network server room and allow only authorized personnel to enter.

**Disaster recovery.** Every outsource vendor must maintain an audited business continuity plan. Any system that has been classified as a mission-critical application must be capable of being restored easily and hardware failures recovered immediately.

The vendor business continuity plan must adequately address the following:

- mission-critical applications and their respective data and server configurations
- maintaining a fully secure, redundant real-time short-range off-site processing environment and system in case of an emergency or system failures in the main facilities

- daily data backup and indefinite storage at a secure off-site facility, preferably an audit-approved facility; data files should be transported using secured and locked containers and tested annually as part of a full network and systems audit
- maintaining a fully operational long-range alternative processing site, tested annually, for use in the event of a regional disaster

### 3. Growth and Brand Protection

Growing your employee benefits business is important to long-term viability. Banking institutions making the decision to outsource retirement plan recordkeeping, administration, and potentially custody and paying agent services should expect their vendors to partner with them to grow the business.

Open-architecture trade platforms, multiple investment product options and services, sales planning consulting, marketing resources, dynamic plan sponsor reviews, customized proposal support, and brand retention and integrity should all be earmarked as vendor requirements.

An outsource vendor should help you grow your business through:

- support of your brand identity on account Web sites, on printed statements, and in communication and selling materials
- opportunities to connect with the vendor's clients to share ideas, develop professional networks, and discuss best selling practices
- development of sales plans and lead-generation programs
- delivery of marketing and sales support materials
- support for proposal writing and face-to-face prospect presentations

### Conclusion

For most banking institutions, the decision to outsource high-cost, low-value operations, boils down to priorities. Banks must focus on what matters most—being a trusted fiduciary partner. Retirement plan recordkeeping doesn't really enhance the value proposition of "trust," but providing higher levels of direct services (e.g., investment reviews and employee meetings) will. ■

### ABOUT THE AUTHOR

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