

FREQUENTLY ASKED QUESTIONS

# Morningstar® ESG Pooled Employer Plan



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## Frequently Asked Questions

### About the Morningstar ESG Pooled Employer Plan

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#### What is the Morningstar ESG Pooled Employer Plan?

The Morningstar ESG Pooled Employer Plan is a retirement plan with an investment lineup that considers financially material ESG factors, created by PAi Trust Company, Inc. (PAi Trust) and Morningstar Investment Management LLC. Read below for more information about pooled employer plans, a new kind of retirement plan made possible with the passage of the Setting Every Community Up for Retirement Enhancement (SECURE) Act, and the responsibilities of PAi and Morningstar Investment Management.

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#### When will the Morningstar ESG Pooled Employer Plan be available?

The Morningstar ESG Pooled Employer Plan is expected to launch early 2022, pending final guidance from the U.S. Department of Labor on the use of environmental, social, and governance (ESG) factors to select investments for retirement plans.

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#### What entities support the Morningstar ESG Pooled Employer Plan?

The main entities involved are the Pooled Plan Provider (PPP), trustee, and 3(38) investment manager. Let's take a closer look at each role:

Role	Entity	Responsibilities
Pooled plan provider (PPP)	PAi Trust Co.	The PPP offers and manages the PEP and selects the necessary service provider and other fiduciaries. The PPP is responsible for recordkeeping, overall administration, custodial services, and other duties.
Trustee	PAi Trust Co.	The trustee is responsible for collecting contributions and holding all the assets that are invested in the PEP.
3(38) investment manager	Morningstar Investment Management LLC	The PPP hires the 3(38) investment manager, who builds and manages the PEP's investment lineup. The 3(38) has discretionary authority to remove and replace funds as needed.

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#### Where can I find information about the Morningstar ESG Pooled Employer Plan?

For more information about the plan, its investment approach, or to speak with a Morningstar Investment Management professional, visit the Morningstar ESG Pooled Employer Plan webpage and complete the contact form. For more information about onboarding and pricing, visit PAi's website or get in touch with PAi's representatives at 800-236-7400.

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#### Who is Morningstar Investment Management LLC?

Morningstar Investment Management is a registered investment adviser and subsidiary of Morningstar, Inc. Our retirement solutions group supports workplace retirement plans and is committed to helping plan participants save for retirement with a range of investment products and services, including a managed accounts service, custom models, target-date products, and fiduciary services.

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#### Who is PAi Trust Company, Inc.?

PAi Trust Company, Inc. (PAi Trust) is a state-chartered public trust company headquartered in South Dakota. PAi Trust and its affiliate PAi are wholly owned subsidiaries of Newport Group, Inc. PAi Trust serves as trustee or custodian on over 17,000 qualified plans and has custody of over \$6.56 billion in retirement assets, including 1,400 IRA accounts.<sup>1</sup>

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#### How is the Morningstar ESG Pooled Employer Plan priced?

Employer Fees	Entity
One-time setup fee	\$390
PAi Trust monthly pooled plan provider and administration fee	\$200/month

Employee Fees	Entity
PAi Trust monthly recordkeeping fee	\$4/month/participant
PAi Trust annual custodial and trading fee	7 bps
PAi Trust annual investment fiduciary fee 5 of the 25 bps go to Morningstar Investment Management	25 bps
Annual intermediary service fee	Set by fee-based advisor

<sup>1</sup> As of 01/01/2021.

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## About the Morningstar ESG Pooled Employer Plan

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### What is a Pooled Employer Plan?

Pooled Employer Plans, or PEPs, are a new kind of retirement plan made possible with the passage of the Setting Every Community Up for Retirement Enhancement (SECURE) Act in December 2019. Made available Jan. 1, 2021, a PEP is a single plan that unrelated employers of any size can join and offer to their employees. Each employer shares the same fund lineup and associated service providers, such as the recordkeeper, fiduciaries, and trustee. Any employer can join a PEP.

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### What are the potential benefits of a PEP?

PEPs are designed to make it easier for businesses, especially small- and mid-sized businesses, to offer a retirement plan by reducing the administrative complexity and fiduciary risk associated with sponsoring a standalone plan. PEPs could also be lower in cost than a standalone retirement plan because of economies of scale, and plan participants may have lower investment fees thanks to having access to share classes that might not be available to smaller plans.

In terms of fiduciary risk, the employer is still responsible for selecting and monitoring the pooled plan provider (PPP), which is the named fiduciary to the PEP and the entity that is responsible for managing and administering the PEP. The PPP is responsible for selecting other service providers, such as the recordkeeper or an investment management firm that builds and manages the plan's investment lineup.

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### Are there any tax credits associated with joining a PEP?

The SECURE Act increased the tax credit for small businesses that start a new 401(k) plan beginning Jan. 1, 2020, and we believe the tax credit will extend to businesses that join a PEP. Before the SECURE Act, a small business could claim a tax credit equal to 50% of their "qualified startup costs," up to a \$500 limit. As of 10/13/2021, the limit is the greater of:

1. \$500, or
2. The lesser of:
  - a. \$250 multiplied by the number of non-Highly Compensated Employees (non-HCEs) eligible for plan participation, or
  - b. \$5,000

This credit is available for up to three years. Subject to change without notice. Neither PAi nor Morningstar Investment Management provide tax advice; we strongly encourage you to visit the IRS site and consult with a tax professional for more information and for eligibility requirements.

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### Are PEPs the same as MEPs?

PEPs are similar to Multiple Employer Plans (MEPs) in that they enable more than one employer to participate in a single retirement plan. However, MEPs require that the employers have a common nexus or organizational relationship. MEPs also have a "one-bad-apple" rule that can cause the entire plan to be disqualified if one employer is noncompliant. Because of these two restrictions, MEPs have experienced limited use in the retirement industry. Meanwhile, PEPs do not have these two restrictions.

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**12****What is a Pooled Plan Provider (PPP)?**

The PPP is the entity that sponsors the PEP. The PPP is responsible for managing and administering the PEP, including hiring other service providers such as the recordkeeper or a 3(38) investment manager. In the case of the Morningstar ESG Pooled Employer Plan, PAi Trust is the PPP.

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**13****What is a 3(38) investment manager?**

The 3(38) investment manager is responsible for building and managing the investment lineup for the PEP and assumes fiduciary responsibility it makes related to the plan lineup. In the case of the Morningstar ESG Pooled Employer Plan, Morningstar Investment Management is the 3(38) investment manager. Morningstar Investment Management is a registered investment adviser and subsidiary of Morningstar Inc.

**Employer Information**

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**14****What are the employers' responsibilities under a PEP?**

As an employer participating in the PEP, you will need to provide employee and employer contributions, as well as proper participant data, to the PPP and/or other service providers in the PEP in a timely manner. To ensure timely contributions, PAi Trust has a tiered fee structure for missed contributions.

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**15****What are my reporting requirements under a PEP?**

As an employer in the PEP, you will still have to complete year-end reporting for testing purposes (example, census information). However, with the PEP, employers will no longer have to file a Form 5500. The PPP will file it on behalf of the entire PEP.

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**16****Do I have any input on how my retirement plan is designed if I select a PEP?**

Every employer that joins the Morningstar ESG Pooled Employer Plan will have the same investment lineup; however, each participating employer has some flexibility over the underlying plan design. For instance, they can determine the vesting schedule, eligibility, or discretionary match within the plan. The Morningstar ESG Pooled Employer Plan cannot accommodate auto escalation, and there are some restrictions around auto-enrollment based on the employer's payroll integration.

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**17****How does a PEP impact my fiduciary responsibilities?**

Employers can offset some of their fiduciary responsibilities by joining a PEP. For instance, the Pooled Plan Provider (PPP) will serve as the named fiduciary on the plan and will assume most of the plan administration duties. The PPP on the Morningstar ESG Pooled Employer plan is PAi Trust. Meanwhile, as the 3(38) investment manager, Morningstar Investment Management will assume fiduciary responsibility for the investments in the lineup. The employer still has a fiduciary responsibility to select and monitor the PPP.

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**18****What ongoing reporting will I receive?**

PAi and Morningstar Investment Management will provide you with the necessary reports to monitor the performance of the lineup and the participants in the plan on a quarterly and annual basis. You'll also receive an Investment Policy Statement that outlines the approach, methodology, and goals of the fund lineup, as well as a market commentary each quarter from Morningstar Investment Management's investment team that offers insights on the overall investment markets. For each fund in the plan's menu, you'll receive a detailed fund report with various performance metrics.

**19****How does payroll deduction work for the Morningstar ESG Pooled Employer Plan?**

The employer will need to provide employee and employer contributions as well as appropriate participant data to the plan in a timely manner. PAi partners with multiple local and nationwide payroll providers to offer an integrated service, which can help reduce some of the administrative tasks of submitting employee contributions. For a full list of payroll providers, visit [pai.com/payroll-integration](https://pai.com/payroll-integration).<sup>2</sup>

**20****Can I have a say in the selection of the PEP's underlying investments?**

No, employers cannot make any investment selections for the Morningstar ESG Pooled Employer Plan. There is a single investment menu — built and managed by Morningstar Investment Management — that every employer in the plan must offer its employees. Investments cannot be added or subtracted from that menu.

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## The ESG Investment Lineup

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### What is sustainable investing (also known as ESG investing)?

Sustainable investing is an investment approach that helps address the potential financial impact of environmental, social, and governance (ESG) factors. These factors can be considered in the investment process to the extent they have a material effect on the risk or performance potential of the security.

The term “ESG” refers to a set of factors—environmental, social, and governance—that are used to analyze a company’s practices and ethics for investment selection purposes:



**Environmental factors** consider how a company performs as a steward of nature, including their waste management procedures, carbon footprint, or pollution.



**Social factors** examine how it manages relationships with employees, suppliers, customers, and the communities where it operates.



**Governance factors** deal with a company’s leadership, executive pay, audits, internal controls, and shareholder rights.

The idea is that by assessing securities for financially material factors, investment professionals can help investors limit potential risks in their portfolios that might otherwise go unnoticed and apply considerations that we know are of growing interest to many investors.

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### Do ESG investments perform as well as non-ESG investments?

Studies have shown that investments that incorporate ESG factors have the potential to deliver comparable and, in some cases, higher returns than those that don’t.<sup>3</sup> Further, 60% of ESG investments have outperformed peers over the last 10 years.<sup>4</sup> The ESG investments selected for this lineup are subject to the same investment selection criteria and review process that we use to select and monitor investments for all retirement plan lineups. Because of this, we believe the investments selected for the Morningstar ESG Pooled Employer Plan are of comparable quality to approved non-ESG investments.

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### What investments are included in the Morningstar ESG Pooled Employer Plan lineup?

We will provide more information about the final lineup the closer we get to the official launch date in the first quarter of 2022.

The plan’s lineup comprises ESG investments that meet Morningstar Investment Management’s rigorous investment selection criteria for retirement investments, plus additional assessments for environmental, social, and governance factors. The funds in the lineup will consider ESG factors—with the exception of certain kinds of investments, such as TIPs or money market funds—that do not have features that would qualify them as ESG-related. ESG factors are not applicable to these types of investments.

The lineup also will include a custom target-date model built and managed by Morningstar Investment Management using the investments selected for the plan’s lineup.

To learn more about how we build ESG lineups, see our [methodology overview document](#).

<sup>3</sup> Gunnar Friede, Timo Busch & Alexander Bassen (2015) ESG and financial performance: aggregated evidence from more than 2000 empirical studies, *Journal of Sustainable Finance & Investment*, 5:4, 210-233, DOI: 10.1080/20430795.2015.1118917

<sup>4</sup> Jon Hale (2020) Sustainable Equity Funds Outperform Traditional Peers in 2020, Morningstar.com, Morningstar, Inc., <https://www.morningstar.com/articles/1017056/sustainable-equity-funds-outperform-traditional-peers-in-2020>

### **What is a custom target-date model and why is one included in the Morningstar ESG Pooled Employer Plan?**

Morningstar Investment Management built a custom target-date model for the Morningstar Pooled Employer Plan in part because the options for target-date funds that consider ESG factors are limited. Further, many target-date funds found in retirement plans are of the “off-the-shelf” variety and typically include in-house proprietary funds managed and sold by the target-date fund provider. Custom target-date models are designed specifically for a plan and allow for more control over the equity glide path and the underlying investments.

The custom target-date model that Morningstar Investment Management has built for the Morningstar ESG Pooled Employer Plan uses our moderate glide path and employs the ESG investments used in the plan’s lineup, which represent our highest conviction selections across the universe of fund managers. The moderate glide path is determined using data that represents the average U.S. investor with an average risk profile and average risk preference. Neither Morningstar Investment Management nor PAi collect any additional fees from the custom target-date model.

### **How does Morningstar Investment Management build custom target-date models?**

Morningstar Investment Management has a dedicated team that has been building and monitoring custom target-date models for more than 10 years. To design the glide path of custom target-date models, we use actual participant data from a variety of government and public sources, as well as our own database of over one million retirement managed accounts users to study actual participant behavior. That data helps us understand how a participant’s total economic situation changes over time. Meanwhile we use several advanced asset-allocation techniques to construct the underlying target-date portfolios. All asset class model portfolios are updated annually, as Morningstar Investment Management reviews and updates the mean variance optimization inputs (expected returns, standard deviations, and cross-correlations) typically during the summer or fall.

With our custom target-date models, our goal is to manage an individual’s wealth throughout their lifetime, from accumulation through retirement, with the aim of maximizing wealth to fund retirement income, preserving the real purchasing power of the accumulated savings, and providing retirement income stability throughout the process.

### **What is the Department of Labor’s stance on ESG?**

Toward the end of the Trump administration, the U.S. Department of Labor issued a rule called “Financial Factors in Selecting Plan Investments” that made it difficult if not impossible for companies to offer funds that used ESG factors in selecting securities for their retirement plans, particularly for qualified defaults. About three months into President Biden’s term, the DOL publicly expressed concern about this midnight rulemaking, noting that ESG factors can play an important role in the evaluation and management of retirement plan investments. The DOL then provided a draft rule in September 2021 that, when finalized, will essentially erase the Trump-era rule and will give companies greater flexibility and freedom to include ESG investments in their retirement plans. We expect the DOL to finalize this guidance in the first quarter of 2022, at which point, we can launch the Morningstar ESG Pooled Employer Plan and begin onboarding plans.

### **Does Morningstar Investment Management or PAi include any proprietary funds in the lineup?**

No, Morningstar Investment Management, PAi Trust, or any of its affiliates do not have proprietary funds within the Morningstar ESG Pooled Employer Plan. Morningstar Investment Management has built a custom target-date model for this lineup, using the same funds in the plan’s lineup; neither Morningstar Investment Management nor PAi derive any additional revenue from this product.



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## About Morningstar Investment Management

Our parent company, Morningstar, Inc., was founded on the simple idea that when people have good investment information, they can make better choices that help them achieve their financial goals. In the retirement solutions group at Morningstar Investment Management LLC, a subsidiary of Morningstar, Inc. and a registered investment adviser, our advocacy for the individual investor extends to the workplace retirement market where the responsibility for investing and saving now rests with employees. We are committed to helping those individuals save for the retirement they want by providing products and services that range from a managed accounts service to custom models to target-date products and fiduciary services.

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