



SO YOU'RE A RETIREMENT PLAN FIDUCIARY...NOW WHAT?

AGENDA

- The Framework
- Defining the Fiduciary
- “The Big 5” - Basic Fiduciary Duties
- Plan Governance
- Limiting Liability
- When Mistakes Happen...Using Correction Programs
- Taking Action!



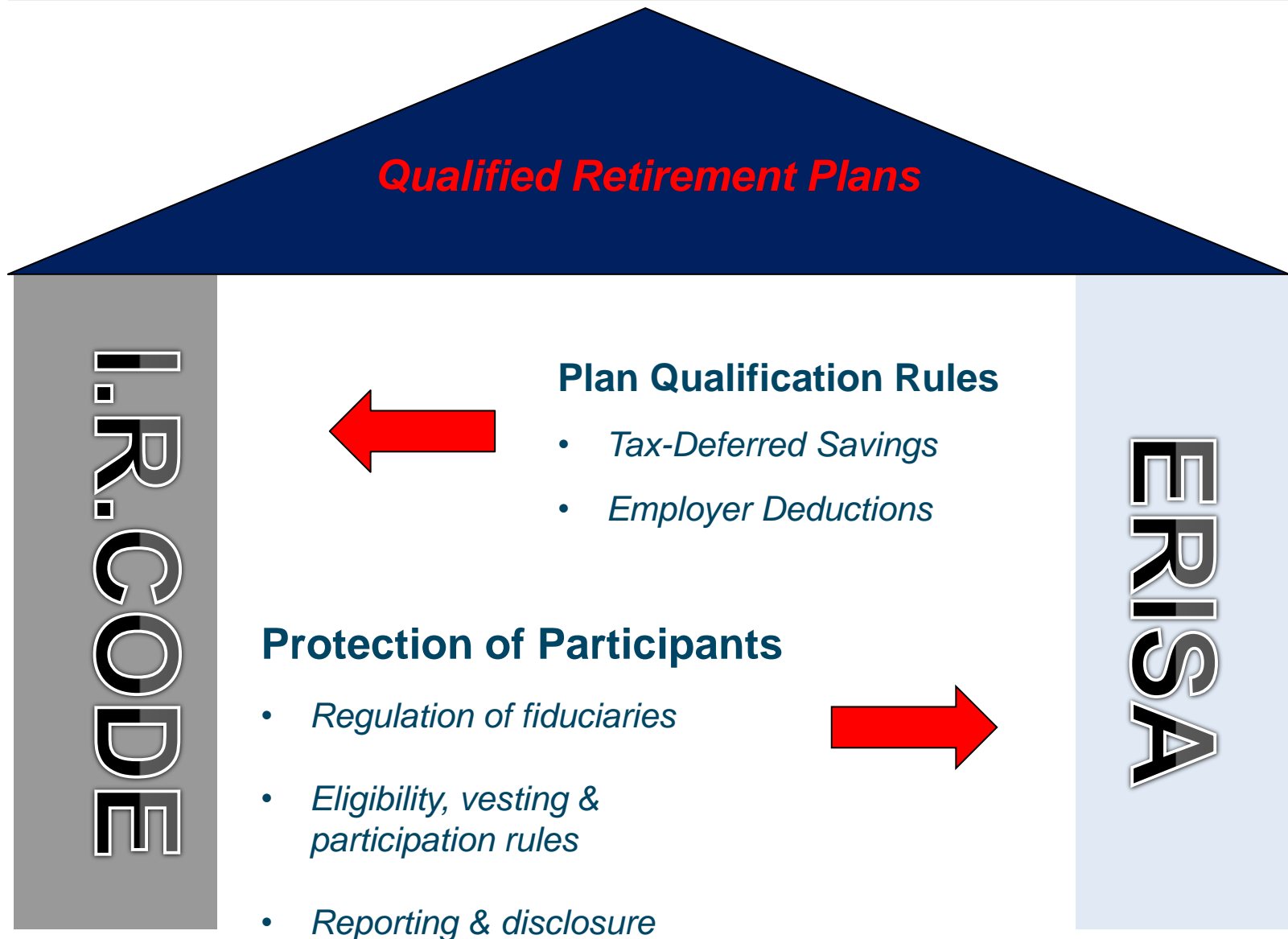
“

Employee benefit plans covered by ERISA are subject to an impressive and somewhat bewildering array of rules and regulations governing their substance and administration as well as their eligibility for favorable tax treatment.

”

Donovan v. Cunningham, U.S. Court of Appeals, Fifth Circuit (October 17, 1983)

The Framework



Fiduciary Responsibility

“a pure heart and empty head” are not enough to satisfy ERISA fiduciary duties*

- ✓ ERISA fiduciaries must understand their duties and responsibilities
- ✓ ERISA fiduciaries can be personally liable for breaches

*Donovan v. Cunningham, 716 F.2d 1455, 1467 (5th Cir. 1983)

Key Elements of a Plan

- ➔ Written plan document describing the structure of plan benefits and operation
- ➔ Plan must have a “named fiduciary” (identified by office or name, can also be a committee)
- ➔ Trust fund for plan assets
- ➔ System for recordkeeping the flow of assets to and from the trust
- ➔ Explanatory documents for plan participants (SPD, SAR, annual notices)
- ➔ Documents to provide information to the government (Internal Revenue Service, Department of Labor, Pension Benefit Guarantee Corporation)



What is a Fiduciary?

- ➔ Generally, a position of trust acting for the benefit of others with a high duty of care and loyalty
- ➔ Under ERISA, any person who exercises **discretionary** authority or control over plan assets or administration, or gives investment advice for a fee

*"Highest duty known to the law."**



*Donovan v. Bierwirth, 680 F.2d 263 (2nd Cir. 1982)

Who is a Fiduciary?

Employer/Plan Sponsor

Plan Administrator

Trustee

Investment Manager

Functional/"Accidental" Fiduciary

Co-Fiduciaries



- ➔ Individuals who serve as fiduciaries for the same plan
- ➔ All fiduciaries have potential liability for the actions of their co-fiduciaries
- ➔ If a fiduciary knowingly participates in another fiduciary's breach, conceals the breach or does not act to correct it, that fiduciary is liable as well
- ➔ Delegation of duties and responsibilities among co-fiduciaries should be defined carefully in writing
- ➔ Each fiduciary should understand from whom and among whom his or her duties have been delegated—to whom he or she is accountable
- ➔ Distinctions among fiduciary positions should be strictly enforced

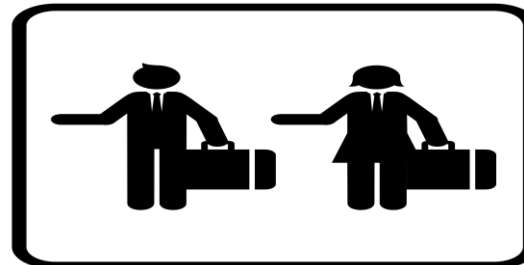
What are the basic duties of a fiduciary?

The “Big 5”

- I. **BE LOYAL.** Act with “an eye single” toward proper plan administration, investment of assets to pay promised benefits to participants and beneficiaries; avoid conflicts of interest and “prohibited transactions” (duty of loyalty)
- II. **BE PRUDENT.** Act with the care, skill, prudence and diligence of a person in a like capacity and familiar with the subject matter. Hire experts where needed, establish and follow well-documented processes
- III. **FOLLOW THE DOCUMENT.** Know and follow the terms of the plan document
- IV. **DIVERSIFY.** Ensure plan investments are diversified to minimize risk and avoid large losses
- V. **CONTROL EXPENSES.** Understand what it costs to administer the plan and pay only reasonable expenses

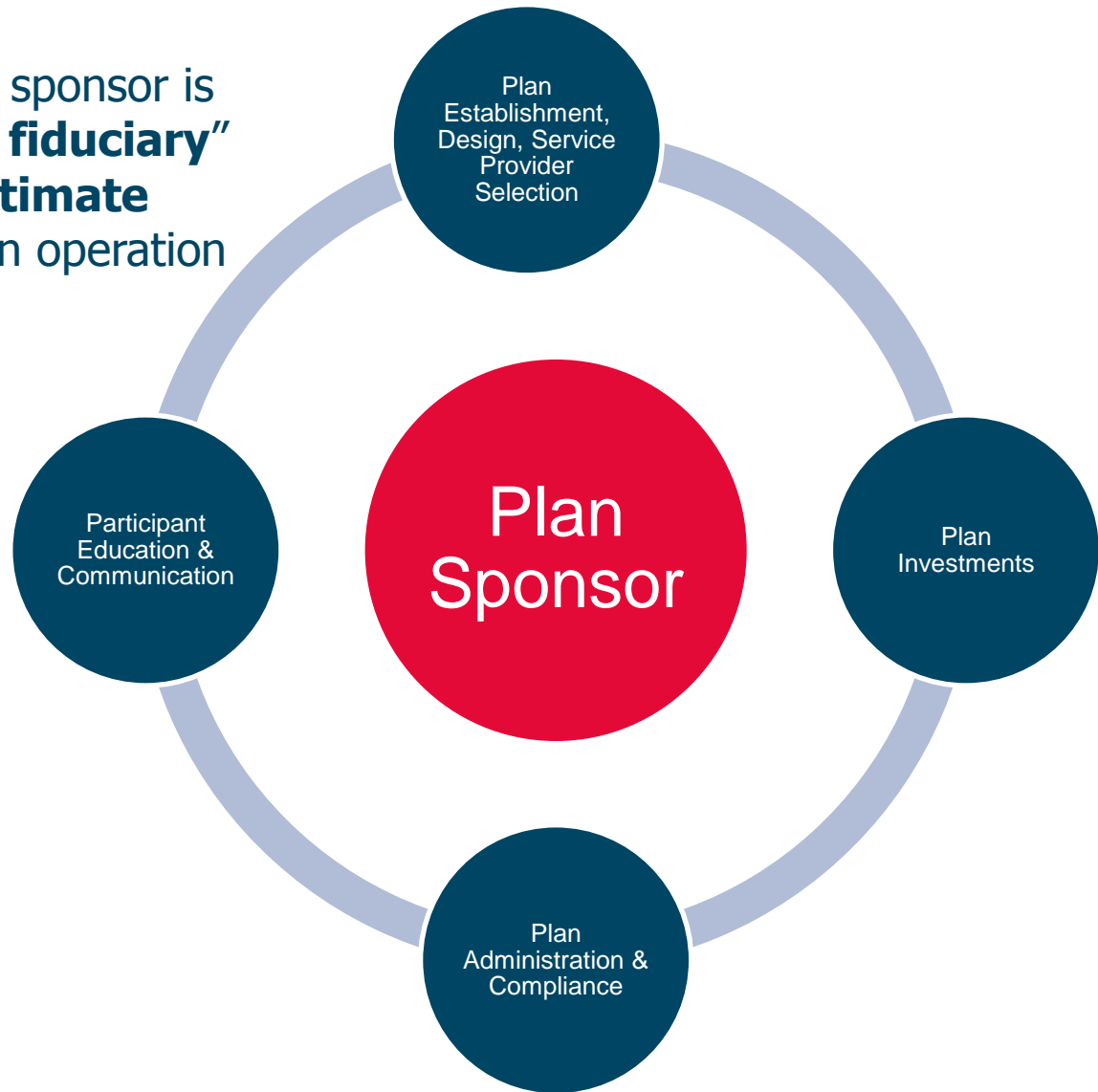
“Settlor” v. Fiduciary Functions

- ➔ Business (“settlor”) decisions are not governed by fiduciary rules
 - ✓ Plan establishment and design
 - ✓ Plan amendments (other than legally required amendments)
 - ✓ Decision to terminate a plan
- ➔ Expenses related to settlor activities may NOT be paid from plan assets
- ➔ **Implementation** of settlor decisions may be fiduciary acts governed by fiduciary rules



Plan Governance

Under ERISA, the plan sponsor is generally the “**named fiduciary**” of the plan with the **ultimate responsibility** for plan operation and administration



Establishing a Plan Governance Structure

- Consider existing corporate governance structure
- Establish a committee/identify responsible parties
- Formal delegation of authority to individuals with “hands-on” responsibilities
- Document duties and responsibilities
- Establish internal controls
- Hold regular meetings
- Provide periodic training
- ***Document, document, document***



Establish Internal Controls

*“An ounce of prevention is worth a pound of cure” definitely applies to keeping retirement plans tax-qualified. Effective internal controls and annual reviews of your plan are essential “ingredients” to prevent costly mistakes that can jeopardize the plan’s tax-favored status.**

- ➔ Maintain documentation of all service provider relationships and fee/service agreements
- ➔ Review plan operations
- ➔ Update plan document as needed
- ➔ Develop policies and procedures e.g.:
 - ✓ Employee Eligibility
 - ✓ Contributions/Payroll Processing
 - ✓ Distributions
 - ✓ Testing and administration
 - ✓ Plan data maintenance
 - ✓ Plan investment selection & monitoring
 - ✓ Employee education & communication
- ➔ ***Document, document, document***



*<https://www.irs.gov/retirement-plans/internal-controls-are-essential-in-retirement-plans>

Delegation of Fiduciary Responsibilities

- ➔ A plan may contain procedures that allow a plan fiduciary to hire service providers to handle certain plan functions
- ➔ Service provider may assume liability for its functions by agreement with the plan
- ➔ Despite this delegation, fiduciaries still retain duty to:
 - ✓ Ensure the service provider understands their responsibilities and has knowledge and information necessary to carry out their duties
 - ✓ Monitor performance on an ongoing basis



Role of Service Providers

Recordkeepers

TPAs*

**Financial
Advisors***

Accountants

Consultants

Attorneys

- *Ministerial functions*
- *Act at the direction of Plan Fiduciaries*
- *No use of discretion*
- *Information provided in professional capacity*

** Financial Advisors and TPAs may assume fiduciary roles in certain cases*

Selecting Service Providers

- ➔ A fiduciary function
- ➔ Evaluate complete and identical information for a meaningful comparison
- ➔ Information to consider:
 - ✓ Information about firm (financial condition, experience with plans of similar size and complexity)
 - ✓ Quality of services (identity, qualifications and experience of persons handling the plan's account, recent litigation)
 - ✓ Description of business practices, existence of liability insurance
 - ✓ Value for quoted fees
- ➔ ***Document, document, document***



Monitoring Service Providers

- ➔ Establish and follow a formal process for review/benchmarking at regular intervals
- ➔ Verify that agreed-upon services are being provided at a satisfactory level through:
 - ✓ Review of provider's performance
 - ✓ Review of reports provided
 - ✓ Audit actual fees charged
 - ✓ Review policies and practices
 - ✓ Follow up on participant complaints
- ➔ Document findings and any related decisions
- ➔ Remember that a fiduciary may be personally liable for a service provider's failure to carry out its responsibilities



Understanding Fees

- ➔ Plan fiduciaries have a duty to ensure that fees and expenses paid by a plan are **reasonable** based on the needs of the plan

- ➔ Compare fees of service providers know what services are needed and the associated costs
 - ✓ **Recordkeeping, administration, participant services**
 - ✓ **Compliance testing and reporting**
 - ✓ **Participant transaction fees**
 - ✓ **Financial professional services**
 - ✓ **Investment fees**
 - ✓ **Other professional fees (accounting, legal)**

- ➔ Remember, all services have costs

- ➔ Know who is paying the fees (employer, plan, participants)

- ➔ Review all service provider fee disclosures

- ➔ Provide required fee disclosures to plan participants



Plan Investments

- ➔ Fiduciaries have a duty to diversify plan investments in order to minimize risk of large investment losses
- ➔ Must understand investments relating to portion of plan assets over which fiduciary has discretion/control
- ➔ Adopt an Investment Policy Statement
- ➔ Hire an “investment manager” with discretion; or
- ➔ Hire service providers with expertise to provide necessary information and/or recommendations to fiduciaries
- ➔ Be sure that plan participants receive adequate investment information and education



Limiting Liability

- ➔ Understand, allocate and delegate responsibilities
- ➔ Know the difference between “fiduciary acts” and non-fiduciary “settlor acts”
- ➔ Follow statutory provisions that provide relief (e.g., ERISA 404(c) for participant directed account plans)
- ➔ Avoid “***prohibited transactions***”
- ➔ Maintain required bonding
- ➔ Consider fiduciary liability insurance
- ➔ Hire an independent fiduciary if needed



Participant Directed Investments – 404(c)

- ➔ 404(c) is an option which provides fiduciaries with a defense against certain participant claims
- ➔ Fiduciaries not liable for individual participant investment decisions if statutory requirements are met
 - ✓ **Participants “exercise control” over investments**
 - ✓ **Must be able to choose from “broad range” of investments (at least 3 options)**
 - ✓ **Must be able to give investment instructions at least quarterly (more often if investment is volatile)**
 - ✓ **Must be given sufficient information to make informed decisions**
- ➔ Fiduciaries are still responsible for selection and ongoing monitoring of plan investment options
- ➔ Qualified Default Investment Alternatives (“QDIA”) provide 404(c) protection where participants do not make affirmative investment choices (automatic enrollment)

What are Prohibited Transactions?

- ➔ Transactions that are directly or indirectly between the plan and a “***party in interest***”
- ➔ Purpose is to protect benefits promised to plan participants and beneficiaries by prohibiting dealings where there are conflicts of interest
- ➔ Even though a transaction might benefit the plan, the increased likelihood of harm to the plan makes it prohibited
- ➔ However, exemptions from certain prohibited transactions do exist under ERISA
- ➔ Department of Labor may grant exemptions upon application

Who are Parties in Interest?

- ⇒ Parties in interest are generally people or entities with a close relationship to the plan
 - ✓ Plan fiduciaries
 - ✓ Sponsoring employer (officers, directors, employees, 50% or greater owners)
 - ✓ Service providers (accountant, recordkeeper, attorney)
 - ✓ Relatives (spouses, ancestors, lineal descendants) of any of the above



What transactions are prohibited?

- ➔ Causing plan to buy, sell or lease property to or from a party in interest
- ➔ Causing plan to receive goods or services from a party in interest
- ➔ Any loan or extension of credit to or from the plan and a party in interest
- ➔ Any use of plan assets to benefit a party in interest
- ➔ Self-dealing with plan assets for a fiduciary's own benefit



Statutory PT Exemption Examples

➔ Service Provider Exemption

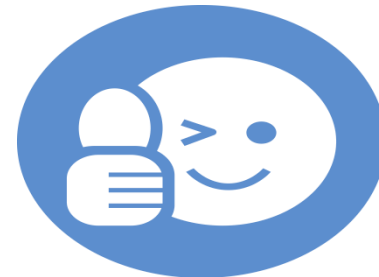
Permits service contracts between parties in interest if:

- ✓ Service is necessary
- ✓ Contract is reasonable
- ✓ Compensation received by service provider is reasonable
- ✓ Service providers have furnished required 408(b)(2) disclosures to responsible plan fiduciaries

➔ Plan Loan Provisions

Allow participants to borrow from a plan if:

- ✓ Available to all participants on a reasonably equivalent basis
- ✓ Made according to plan provisions
- ✓ Interest rate is reasonable
- ✓ Loan is adequately secured



Class and Individual Exemption Examples

- ➔ Class exemptions apply broadly to specified transactions or a specified industry
 - ✓ Relief from excise taxes for correction of certain ERISA violations corrected under DOL correction program (VFCEP)
 - ✓ To use this exemption, all potential violations must be understood and all conditions of the class exemption must be met

- ➔ Individual exemptions apply to a specific plan
 - ✓ Individual application to DOL is required
 - ✓ Example: plan owns a parcel of real estate and wishes to sell it to a party in interest
 - ✓ If the individual exemption is granted, all conditions of the exemption must be met

Bonding Requirements

- ➔ Plan must be covered by a fidelity bond
 - ✓ Lesser of 10% of plan assets or \$500,000 (\$1,000,000 if the plan holds employer securities)
- ➔ Covers fiduciaries and those who handle plan assets or other plan property
- ➔ Protects the plan against losses due to fraudulent or dishonest acts of those covered by the bond
- ➔ Different than fiduciary liability insurance



Fiduciary Liability Insurance



- ➔ Different from required ERISA fiduciary bonding
- ➔ Purchased at the option of the employer
- ➔ Provides protection to employer/sponsor and officers, directors and employees
- ➔ Coverage provided for breaches of fiduciary duties under ERISA (prohibited transactions, self-dealing, failure to diversify investments, conflicts of interest)
- ➔ Typically does not cover service providers
- ➔ Available as both a stand-alone product or as an add-on to D&O coverage

Correction Programs

- ➔ ERISA or Internal Revenue Code violations discovered through DOL or IRS audit may result in penalties and, in extreme cases, plan disqualification
- ➔ DOL and IRS advocate voluntary compliance and encourage review plan operations for compliance
- ➔ DOL and IRS correction programs exist to help with voluntary correction with reduced fees and penalties



Correction Programs

- ➔ DOL Voluntary Fiduciary Correction Program (“VFCP”)
 - ✓ **For correction of certain violations under ERISA (e.g., late deposit of employee deferrals, improper payment of “settlor expenses” with plan assets)**
- ➔ DOL Delinquent Filer Voluntary Correction Program (“DFVCP”)
 - ✓ **Correction of failure to timely file form 5500**
- ➔ IRS Employee Plans Compliance Resolution System (“EPCRS”)
 - ✓ **Correction of plan defects under IRS rules for tax-qualification (e.g., failure to adopt plan amendments timely, failure to perform plan coverage and nondiscrimination testing)**



Action Steps for Plan Fiduciaries

- ➔ Verify all fiduciaries have been properly appointed, accepted and understand responsibilities
- ➔ Provide training for fiduciaries and anyone else who deals with the plan
- ➔ Establish and follow a “plan governance structure” (internal controls, meetings, decision making processes, calendars, checklists, monitoring of service providers and fees, roles and responsibilities)
- ➔ Hire experts where needed, delegate as necessary
- ➔ Review and understand the plan document
- ➔ Ensure administration coincides with plan provisions



Action Steps for Plan Fiduciaries

- Establish and review investment policy statement and process for ongoing monitoring of plan investments
- Operate participant-directed investment plans in a manner that satisfies ERISA Section 404(c)
- Communicate plan procedures for enrollment, plan transactions and investments to plan participants
- Monitor plan service providers on a regular basis
- Conduct periodic self-audits
- Use DOL and IRS correction programs where necessary
- Consider purchase of fiduciary liability coverage
- ***Document, document, document!***



Resources

- ➔ DOL Employee Benefits Security Administration
<http://www.dol.gov/ebsa/>
- ➔ EBSA Fiduciary Education Campaign
<http://www.dol.gov/ebsa/fiduciaryeducation.html>
- ➔ Internal Revenue Service – Retirement Plans Community
<http://www.irs.gov/retirement/index.html?navmenu=menu1>

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