June 26-29, 2011
Las Vegas, Nevada

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SOCIETY FOR HUMAN RESOURCE MANAGEMENT

# ERISA Fiduciary Obligations: How to Protect Yourself, Your Boss and the Company

**Sheldon J. Blumling • June 27, 2011**

SHRM 2011 Annual Conference & Exposition

- Fiduciary—
  - > An individual in whom another has placed the *utmost trust and confidence* to manage and protect property or money.
  - > The relationship wherein one person has an obligation to act *for another's benefit.*

— http://legal-dictionary.thefreedictionary.com/fiduciary

## Today's Agenda:

- Understanding ERISA Fiduciary Obligations
  - > ERISA 101 (the short course…)
  - > Who is a fiduciary under ERISA?
  - > General fiduciary obligations
  - > Types of fiduciary liability
- Real World Scenarios
- How to Protect Yourself, Your Boss and the Company
- Questions

- ERISA 101 (the short course…)
  - > Federal law governing *most* employee benefit plans and arrangements
    - Retirement plans
      - – 401(k) plans
      - – Profit sharing plans
      - – Defined benefit pension plans
    - Health and welfare plans
      - – Medical, dental and vision plans
      - – Life and disability insurance plans
      - – Some EAPs, wellness programs and severance plans
    - Exceptions
      - – Most vacation, sick and other leave programs
      - – Most cash and equity incentive plans

- ERISA 101 (the short course…)
  - > Creates consistent regulatory scheme for administering employee benefits in multiple states
  - > Generally preempts State law other than insurance law
    - Insurance law exception is a BIG exception
    - Preemption helps employers by:
      - – Preventing *most* State law mandates, other than insurance law mandates
      - – Establishing limited and exclusive civil enforcement provisions

- ERISA 101 (the short course…)
  - > Does *not* require employers to establish employee benefit plans or arrangements
  - > However, if you do…
    - Minimum standards
      - – Retirement plan participation, vesting, accrual and funding requirements
      - – Health plan requirements like COBRA coverage, HIPAA portability and many of the new healthcare reform requirements
    - Reporting and disclosure requirements
      - – Summary plan descriptions (SPDs)
      - – 5500 Annual Returns
    - Fiduciary obligations

- ERISA 101 (the short course…)
  > Keep in mind…
    - Much of ERISA was drafted with defined benefit pension plans in mind
    - Nonetheless, ERISA applies equally to defined contribution retirement plans (401(k) plans, profit sharing plans, etc.) and health and welfare plans

- Who is a fiduciary under ERISA?
  - > Statutory definition—[A] person is a fiduciary with respect to a plan to the extent **(i)** he exercises any *discretionary authority or discretionary control* respecting management of such plan or exercises any *authority or control* respecting management or disposition of its assets, (ii) he renders investment advice for a fee or other compensation, direct or indirect, with respect to any moneys or other property of such plan, or has any authority or responsibility to do so, or **(iii)** he has any authority or discretionary responsibility in the administration of such plan.

- Who is a fiduciary under ERISA?
  - > Those who have or exercise discretion in the administration of an employee benefit plan
  - > Those who exercise control of plan assets
  - > Investment professionals
  - > Designated “named fiduciaries”

- Who is a fiduciary under ERISA?
  - > Those who have or exercise discretion in the administration of an employee benefit plan
    - Administering plan eligibility requirements
    - Determining plan benefits
    - Interpreting plan terms and provisions
  - > Those who exercise control of plan assets
    - Calculating and remitting plan premiums or contributions
    - Authorizing plan distributions
- Keep in mind…
  - > Actual authority and actions/functions generally are more important than titles

- General fiduciary obligations
  - Statutory "Prudent Man Standard of Care"—[A] fiduciary shall discharge his duties with respect to a plan solely in the interest of the participants and beneficiaries and (A) for the exclusive purpose of: (i) providing benefits to participants and their beneficiaries; and (ii) defraying reasonable expenses of administering the plan; (B) with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims; (C) by diversifying the investments of the plan so as to minimize the risk of large losses, unless under the circumstances it is clearly prudent not to do so; and (D) in accordance with the [plan documents] insofar as such [documents] are consistent with the provisions of [ERISA].

- General fiduciary obligations
  - > Statutory “Prudent Man Standard of Care”
    - Act solely in the interest of plan participants and beneficiaries with the exclusive purpose of providing plan benefits
    - Carry out duties in a prudent manner applicable to the situation
    - Ensure that plan expenses are reasonable
    - Follow plan documents and ERISA
    - Diversify plan assets

- General fiduciary obligations
  - > In addition to statutory "Prudent Man Standard of Care"…
    - Plans must be set forth in writing and consistent with ERISA
    - Generally, plan assets must be held in trust and may not inure to the benefit of the employer
    - "New" disclosure requirements for participant-directed individual account plans
      - – Plan procedures for directing investments
      - – Plan expenses
      - – Investment information, including performance data, benchmarks, fees and expenses
      - – Strict timing and format requirements

- General fiduciary obligations
  - > In addition to statutory "Prudent Man Standard of Care"…
    - Avoiding "prohibited transactions"
      - – Transactions between plans and related parties
        - – Related parties include fiduciaries, service providers, the employer, etc.
        - – Sale, exchange or leasing of property
        - – Lending of money or other extension of credit
      - – Dealing with plan assets in a fiduciary's own interest or for the fiduciary's own account
      - – Statutory and regulatory exemptions

- Fiduciary actions/decisions vs. “settlor” (business) actions/decisions
  - > “Settlor” concept derived from trust law
  - > Establishing, amending and terminating a plan are settlor/business actions/decisions
  - > Once a plan is established, administering it involves fiduciary actions/decisions
- HR and others typically wear both a “business hat” and a “fiduciary hat”
  - > Important to recognize which hat you are wearing when taking actions and making decisions

- Types of fiduciary liability
  - > Restore plan losses resulting from a breach
  - > Disgorge profits resulting from a breach
  - > “Other equitable or remedial relief…, including removal”
  - > Civil penalties under ERISA
  - > Prohibited transactions
    - Unwind or reverse the transaction
    - Penalties

- Types of fiduciary liability
  - > Personal liability
  - > Joint liability for breaches by other plan fiduciaries
    - If you knowingly participate in or conceal a breach of another fiduciary
    - If you enable the breach of another fiduciary by failing to adhere to the "Prudent Man Standard of Care"
    - If you know of the breach of another fiduciary, unless you make reasonable efforts under the circumstances to remedy the breach
    - Bottom line—everyone gets sued
  - > Who pursues fiduciary liability?
    - U.S. Department of Labor (through audits and lawsuits)
    - Aggrieved or harmed participants or beneficiaries
    - Other fiduciaries
    - Plaintiffs lawyers…

- Real World Scenarios
  - > Administering plan eligibility provisions
    - Notifying plan participants about eligibility
    - Administering eligibility classifications, such as part-time vs. full-time employees
  - > Transmitting 401(k) contributions and participant loan payments to the trust
    - A favorite of the U.S. Department of Labor
    - The de facto “as soon as possible” standard
    - 7 business-day safe harbor for small plans (fewer than 100 participants)

- Real World Scenarios
  - > Understanding plan expenses
    - Vendors that administer 401(k) plans "for free"
    - Direct expenses vs. indirect or "soft dollar" expenses
    - Investment fund expense ratios
    - Help is on its way as a result of new DOL Regulations
  - > Paying expenses with plan assets
    - "Settlor" expenses vs. appropriate plan expenses
    - Allocation of plan expenses among participant accounts
    - Charging individual plan participants certain expenses, such as QDRO and plan loan expenses

- Real World Scenarios
  - > Vendor RFPs
    - Doing them to ensure expenses are reasonable for the given market
    - “Brother-in-law” issues…
    - “Vendor relations” issues
  - > Plan investments
    - Company-directed
    - Participant-directed
      - – “404(c) plans” and QDIAs
      - – Still “on the hook” for the investment menu
    - Professional investment advice
  - > Compliance issues
    - Correcting plan errors
    - Maintaining tax-qualified status of retirement plans

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- Understand your obligations
  - > Fiduciary education/training
  - > DOL publication "Meeting Your Fiduciary Responsibilities" (http://www.dol.gov/ebsa/fiduciaryeducation.html)
- Add structure to the process and actually follow it
  - > Plan administration procedures
  - > Plan committees
    - Claims and appeals
    - Plan investments
  - > Dust off the documents and be sure they are consistent with plan operation

# ERISA Fiduciary Obligations: How to Protect Yourself, Your Boss and the Company



- Document, document, document…
  - > The "Prudent Man Standard of Care" does not require perfect results
  - > Documentation supports that the Standard of Care was met
    - Claims files
    - Minutes from committee meetings
    - Fiduciary education/training
- ERISA fidelity bonds and fiduciary insurance

- Take steps to comply with ERISA section 404(c)
  - > Provide participants with an opportunity to exercise control over assets in their accounts, subject to reasonable restrictions
  - > Offer an appropriately broad range of investment alternatives
  - > A participant must actually have exercised independent control with respect to the investment at issue
  - > Satisfy specific disclosure requirements
- Establish a Qualified Default Investment Alternative (QDIA)

# ERISA Fiduciary Obligations: How to Protect Yourself, Your Boss and the Company



- Regularly monitor plan vendors and investments, and understand and monitor plan expenses
  - > Plan vendors
    - Periodic RFPs
    - Avoid potential conflicts of interest
    - Understand and monitor plan expenses
  - > Plan investments
    - Get appropriate professional advice
      - – Follow appropriate advice
      - – Consider outsourcing investment management
    - Regular, periodic reviews
    - Employer stock

# ERISA Fiduciary Obligations: How to Protect Yourself, Your Boss and the Company



- Regularly monitor plan vendors and investments, and understand and monitor plan expenses
  - > Vendor and investment contracts
    - The “devil is in the details”…
    - Watch out for:
      - – Aggressive disclaimers
      - – Gratuitous representations and warranties
      - – Lopsided and/or very limited indemnifications
      - – Termination restrictions and/or fees
    - Have reviewed by counsel with ERISA knowledge
    - No such thing as a “standard contract” or “required boilerplate”—within reason, everything is negotiable

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# Questions ???

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