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Retirement Plan Governance: UNDERSTANDING THE ROLE OF A BENEFIT PLAN COMMITTEE

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All investments involve risk, including possible loss of principal.

IMPORTANT NOTE: The Wagner Law Group has prepared this white paper on behalf of Legg Mason & Co., LLC. This paper includes suggested practices that plan sponsors, and the financial professionals who work with plan sponsors, may wish to consider in connection with the management of the plan and its investments.

It is important to note that the suggested practices are not the exclusive means of managing plan investments, monitoring the fees of service providers or delivering participant education. Other combinations of practices also may be effective. Plan sponsors and other fiduciaries should consult with their own legal counsel concerning their responsibilities under ERISA in the administration and management of their respective plans.

Future legislative or regulatory developments may significantly impact these suggested practices and the related matters discussed in this paper. Please be sure to consult with your own legal counsel concerning the application of the Employee Retirement Income Security Act of 1974 (ERISA) to the selection of plan investments and any related future developments.

This white paper is intended for general informational purposes only, and it does not constitute legal, tax or investment advice on the part of The Wagner Law Group or Legg Mason & Co., LLC and its affiliates. Plan sponsors and other fiduciaries should consult with their own legal counsel to understand the nature and scope of their responsibilities under ERISA and other applicable law.

The content of this white paper was updated in June 2020 and is subject to change.

INVESTMENT PRODUCTS: NOT FDIC INSURED • NO BANK GUARANTEE • MAY LOSE VALUE

FIDUCIARY AUTHORITY AND RESPONSIBILITY

Retirement plan sponsors and other plan fiduciaries face harsh consequences if they fail to satisfy the stringent standards mandated by ERISA. The best way for fiduciaries to meet their responsibilities and to defend against the severe penalties imposed for ERISA violations is to develop a clear awareness and understanding of what those fiduciary responsibilities are. With knowledge of what they are charged to do, fiduciaries may then be vigilant in ensuring that the plan operates consistent with the high standards of ERISA. As explained below, the benefit plan committee is the party whose actions are critical for minimizing potential exposure to fiduciary violations that could lead to Department of Labor enforcement actions and/or private litigation.

Who is a fiduciary?

A person becomes a fiduciary to a plan – and therefore has fiduciary responsibilities to that plan – if he or she (i) 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) 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) has any discretionary authority or discretionary responsibility in the administration of such plan.[1]

In short, a fiduciary is anyone who is authorized to use his or her own judgment to make important decisions about the plan, whether that is about how the plan is administered or what investments it makes.

A fiduciary owes to the plan the highest duty of care imposed by law. A fiduciary must: (i) act for the "exclusive purpose" of the plan; (ii) act with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in like capacity and familiar with such matters would use under the circumstances; (iii) "diversify" plan investments; and, (iv) act in accordance with the "terms of the plan," unless contrary to ERISA.[2]

A fiduciary may be held personally liable for breaching the fiduciary duties owed to a plan.[3] A fiduciary may be required to pay for any losses suffered by a plan because of his or her breach, be forced to restore any profits made by using the plan assets and is subject to a host of fines and penalties.

Who is the Named Fiduciary?

The fiduciary with the authority to control and manage the operation and administration of the plan must be named or identified in the plan's written document.[4] This Named Fiduciary, which has primary fiduciary authority over the plan as well as control over plan investment matters, does not need to be the employer sponsoring the plan. As a practical matter, many plan sponsors are inclined to retain control over the plan's operation so the plan document frequently names the employer as the Named Fiduciary.[5]

Many employers prefer to have the comfort of knowing that their plans have the attention of a dedicated team of trusted employees. The plan document may provide a process to identify an internal committee made up of officers and employees to act as the Named Fiduciary. Even when Named Fiduciary status is retained by the plan sponsor, it may delegate those responsibilities to a committee whose members will themselves be fiduciaries.

Who is the plan Administrator?

It is customary in traditional arrangements for the plan document to also name the plan sponsor as the plan's Administrator as defined under ERISA Section 3(16). The term "Administrator" when used in this sense refers to a special type of fiduciary who has key reporting and disclosure responsibilities under ERISA. The Administrator is responsible for the plan's annual regulatory filings on Form 5500 and for engaging an accounting firm to audit the plan's financials as necessary.[6] In addition to these reporting duties, the Administrator is also responsible for providing summary plan descriptions and other required disclosures to participants.

The Administrator alone is subject to statutory penalties for any violation of ERISA's reporting or disclosure requirements, even if it relies on a third-party provider to help it discharge its reporting and disclosure duties.[7]

The Administrator also has the very important role of appointing all service providers to the plan. This decision must be made carefully, with due consideration of the services to be performed, the qualifications of the provider and the fees to be charged.

Responsibilities do not end with the sound selection of a provider. The Administrator has the ongoing duty to monitor the activities of all providers to ensure that they are fulfilling their commitments to the plan and that they are doing so in a manner the meets that requirements of ERISA.

As in the case of the responsibilities of a Named Fiduciary, the Administrator's responsibilities may be delegated to a committee.

[1] ERISA Section 3(21)(A).
[2] ERISA Section 404.
[3] ERISA Section 409.
[4] ERISA Section 402(a)(1).
[5] For purposes of this guide, all references to a "plan sponsor" are generally references to a plan sponsor that has assumed the role of the plan's Named Fiduciary.
[6] 29 CFR § 2520.103-1.
[7] To neutralize a portion of the revenue loss expected to result from the benefits it enhanced, the SECURE Act increased by tenfold the penalty for failure to file Form 5500 to $250 per day, up to a maximum of $150,000. H.R. 1994, Section 403.

PLAN COMMITTEE **ORGANIZATION**

Committee Membership

Plan sponsors must seriously consider the structure and personnel of a committee that oversees a plan and undertakes the functions of a Named Fiduciary. ERISA includes provisions intended to avoid the situation where members of a plan committee cannot be identified and so escape responsibility and liability. Thus, either the specific persons who are members of the committee must be named in the plan document or the means by which the members will be selected must be clearly stated.

The first matter that should be decided is the nature of the committee's workload and whether more than one committee should be established to handle it. Investment matters (including the structure of the investment menu for plans that permit participant-directed investments, the development of an investment policy statement and the monitoring of investment performance) are sometimes assigned to a separate committee populated with officers and employees of the plan sponsor who have financial expertise. This group may also be responsible for hiring and evaluating the performance of other plan vendors, such as the recordkeeper, investment advisor and other service providers.

The design and operation of the plan is another set of functions that may include government reporting as well as employee communications and education. The responsibilities of a committee overseeing these matters may also entail establishing uniform policies and procedures, as well as rules for determining benefit eligibility. It might oversee the plan's claims procedure and loan programs. Certain committees may also have the function of identifying any need for technical, clarifying or legally required plan amendments and must adjust plan procedures as needed.

The membership of the committee (or committees) should be large enough to handle the assigned workload but not so large as to make it unmanageable. A committee consisting of three to seven members is often considered to be the most efficient.

It is usually inadvisable to name specific individuals to the committee, since their resignation or death would create a vacancy and impede the committee's work if the vacancy is not filled. Accordingly, the plan document sometimes designates plan committee members by the function they perform for the plan sponsor. For example, the heads of the employer's Finance, Human Resources and Legal divisions would automatically assume committee membership. Alternatively, a process for appointing committee members may be stated in the plan document. Some plan sponsors designate plan committee members by title, taking the position that this is a settlor function rather than a fiduciary function. Arguably, however, appointing required committee members is sufficiently similar to hiring a service provider, which is seen as a fiduciary function.

A view that seems to be gaining more adherents is that committee members should have term limits. Rotating committee membership has the advantage of bringing fresh perspectives to committee deliberations. However, an effort to retain continuity and institutional knowledge should be made by staggering terms so that experienced members are always part of the mix. Training materials should be made available to new members to apprise them of fundamental fiduciary principles and key issues faced by the committee.

Committee Charter

To ensure that the committee understands its role, it would be useful to formalize its mission, as well as its structure, in a plan committee charter. The statement of the committee's duties should be flexible enough to allow it to fulfill any additional responsibilities as may be delegated to it from time to time by the plan sponsor, its board of directors or the plan's Named Fiduciary, if the committee is not itself designated as the Named Fiduciary.

A charter can also state the rules for committee governance by stipulating that regular committee meetings be held at intervals that are either stated in the charter or determined in some other manner authorized by the charter, such as at the direction of the committee chair. A charter can also establish the rules for establishing a quorum and may clarify whether members may participate in a meeting by means of electronic communication.

Records of Meetings

Written records should be kept of committee meetings and fiduciary-related decision making, such as the reason for hiring any investment professional or other service provider. This supports the critical requirement that the committee exercise procedural prudence under ERISA.

A charter can ensure that this writing requirement is part of the committee's basic operating procedures. Although a committee charter is often very helpful, keep in mind that it is also a document under which a plan operates, so it must be carefully followed.

COMMITTEE MEETINGS

As noted, a plan committee should meet on a regular basis. The meetings should be used to not only address immediate issues but also as a way to meet the plan's long-term goals. Therefore, meeting agendas should be set in advance to cover specific administrative issues of the day as well as long-term strategic questions, such as the plan's role in the plan sponsor's overall compensation structure, the effectiveness of its design, retirement readiness of participants, and efficient utilization of available investment products and services.

To maximize the usefulness of committee meetings, the agenda should be distributed to committee members and their staffs in advance of the meeting. This will also facilitate documenting the matters to be discussed at the meeting. It is a best practice for certain topics, such as investment performance, to be addressed at least semi-annually.

Representatives from the plan's various service providers should attend meetings that focus on their areas of expertise and be prepared to answer questions from the committee members. For example, outside actuaries, accountants, lawyers, recordkeepers investment advisors and benefits consultants should participate in meetings where their work for the plan will be considered. It is not common practice to include these outsiders on the committee. The scope of the committee's questions should extend to developments in the disciplines of the plan providers attending the meeting that have the potential to affect the plan. This will provide the committee with a sense of the potential issues that will need to be addressed in the future and enable it to set an agenda for the coming year. For example, legal specialists and accountants can provide their knowledge about issues likely to be the focus of a Department of Labor (DOL), Pension of Benefit Guaranty Corporation (PBGC), or Internal Revenue Service (IRS) audit and the materials that should be maintained to meet document requests by investigators from these agencies, as well as new regulatory guidance and issues arising from fiduciary litigation.

The committee's interaction with service providers is also a good way to sort out which provider is responsible for various plan duties. Committee members will need to understand the terms and benefit formulas of the plans for which the committee is responsible so that they can determine what needs to be done and by whom. A table suggesting a list of agenda items, as well as periods to review those actions, follows on the next page.

Investment Committee Meeting
Suggested Agenda Items

Each Meeting
(not every action must be conducted at every meeting but the committee should confirm, via appropriate reports, that each action has taken place each quarter)

- Review and approve minutes of last meeting
- Review quarterly plan investments performance report (presented by advisor, if available)
  - Review performance of each investment
    - Rate of return over not less than 1-, 3- and 5-year periods
    - Compare to appropriate benchmark and peer funds
    - Monitor for style drift
  - Discuss any significant developments, such as change in ownership or fund manager, disciplinary actions
  - Confirm that each option is consistent with Investment Policy Statement criteria
  - Evaluate investments on watch list, if any, and add any new investments
  - Review investment menu for offering a properly diversified array of options
- Review custodian's account statement and compare to advisor's report; resolve any differences
- Vote proxies for shares of investments
- Review fee computations for accuracy
- Review plan operations
  - Confirm that all contributions are deposited in a timely fashion and correctly
  - Confirm that all distributions are correct and were properly authorized
  - Review numbers and status of plan loans and hardship withdrawals
- Plan agenda for next committee meeting

At Least Once Per Year
(these actions may be scheduled for specific meetings throughout the year)

- Conduct fiduciary and investment education for committee, which may include information about the plan; general financial, investment, retirement information; asset allocation models; and interactive investment materials. Focus at least on fiduciary standards, duties and responsibilities.
- Review all fees for reasonableness and compliance with service providers' contracts
- Confirm that all services contracted for are being performed
- Confirm that ERISA bond, fiduciary liability insurance, Directors' and Officers' Liability insurance is in place with appropriate limits
- Review approach for how costs are allocated among participant's accounts
- Confirm that no payment has been made from plan assets for settlor services (i.e., consulting about amending the plan, terminating the plan or creating a new plan)
- If 404(c) relief is sought, confirm that plan complies with requirements
- Confirm receipt of advisor's Form ADV; review conflicts of interest (including additional sources of compensation), trading practices, best execution, and disciplinary actions
- Confirm receipt, review of and proper filing of any investment prospectuses, statements of annual report, annual reports
- Review proxy voting record of each investment option
- Welcome new committee members and conduct orientation

Periodically

- Issue new requests for proposals for service providers
- Evaluate success of participant education programs
- Evaluate participants' readiness to retire

SELECTING
PLAN PROVIDERS

Establishing reasonableness

Plan committees typically have the duty to hire, monitor and fire those who provide any services to the plan. This includes any investment advisor appointed to help the committee, the recordkeeper, any third-party administrator, the custodian of the funds, and anyone else who is paid from plan assets.

ERISA prohibits a fiduciary from approving any contract to provide services to a plan unless it first determines that the service is necessary for the establishment or operation of the plan, the contract for the service is reasonable, and no more than reasonable compensation is paid for the service.[8]

Plan committees need extensive information to meet these requirements. Only then can a committee meet its duty to determine whether the investment itself and the fees charged for it are reasonable. Because of this, the DOL implemented a rule in 2012 which makes any contract for service per se unreasonable unless the service provider makes extensive disclosures describing the services to be provided, the compensation to be charged, and whether it acts as a fiduciary.[9]

Named after the section of ERISA that requires them, the disclosures concerning services and fees are known as the "408(b)(2) disclosures." This information is extensive and can be complex. A plan committee may need the help of its financial advisor to interpret them and explain their significance.

Settlor Services

The DOL recently launched some new examination issues that pose a significant trap for the unwary. These new claims are based on old laws concerning "settlor" services.

ERISA is based on legal concepts developed over time about how trusts should operate. Included among them is the principle that the creator of a trust, called the "settlor," has his or her own purposes for establishing and maintaining the trust that are unrelated to operating that trust for the benefit of its beneficiaries. The settlor pays its own expenses when establishing the trust and does not charge those expenses against trust assets.

The DOL examined this construct some years ago and released guidance to plan sponsors.[10] In short, a plan sponsor is believed to be motivated to create a plan to meet its own business needs, such as recruiting, rewarding and retaining its employees who are plan participants. Hence, expenses such as legal and consulting fees arising from designing the plan, amending or creating new, discretionary features of a plan, or terminating a plan, belong to the employer as its own business expenses. Only fees relating to the ongoing maintenance and tax-qualification of a plan may be charged against plan assets. These non-settlor administrative expenses actually benefit the plan participants and can be offset from trust assets that would otherwise be used to pay benefits. Permitted administrative expenses include reporting and auditing costs, third-party administrator fees, legal and other fees related to amendments needed to keep the plan qualified, and investment-related services.

Very little enforcement activity relating to settlor services has occurred. Recently, however, the DOL has explored these concepts in examinations and a new target for potential violations may follow.

Plan committees are cautioned to seek competent legal advice to guide them about what charges can be assessed against their plans and what are in fact settlor expenses. Unknowingly permitting plan assets to be charged for what are the employer's own costs is a serious breach of fiduciary duty and can lead to significant penalties.

[8] 29 CFR § 2550.408b-2.

[9] 29 CFR § 2550.408b-2(c)(1)(i).

[10] DOL Advisory Opinion 2001-01A; Advisory Opinion 1997-03A.

SELECTING
PLAN INVESTMENTS

Investment policy statement

One of a plan committee's principal duties is to select and review the plan's investments or, in the case of a defined contribution plan with participant direction of investments, select the plan menu. It is a common and best practice to follow the guidelines laid out in the plan's investment policy statement ("IPS").

An IPS is a written statement designed to further the purposes of the plan by providing a set of principles to guide the plan's fiduciaries in managing the plan's investments.[11] According to the DOL, maintaining an IPS is consistent with a plan sponsor's fiduciary obligations under ERISA, including the "duty of loyalty" under ERISA Section 404(a)(1)(A) and the "duty of prudence" under ERISA Section 404(a)(1)(B). It is highly recommended that a plan sponsor formulate an IPS and periodically revise it to fit changing circumstances. Financial advisors who work with plan sponsors should strongly recommend that they do so and be prepared to render assistance in developing guidelines meeting each plan's particular needs.

There are no definitive rules about the content of an IPS. An IPS customarily addresses: (1) the plan's investment objectives, (2) the roles and responsibilities of particular plan fiduciaries, (3) guidelines for selecting, monitoring and changing investment options, and (4) participant communications and investment education. With respect to the asset classes of investments covered by the plan's menu, the IPS should contemplate a broad range of investment categories that satisfy the fiduciary requirements discussed below.

In creating an IPS, a plan committee should consider only those factors that relate to the economic interest of plan participants and the demographics of the overall plan population. Determining the terms of an IPS is itself an exercise of fiduciary responsibility and, as such, the IPS should take into account the duty of prudence and other fiduciary requirements under ERISA.[12]

Since an IPS is part of the "documents and instruments governing the plan" for purposes of ERISA Section 404(a)(1)(D), plan fiduciaries are obligated to follow the terms of the IPS in order to meet their duty to comply with the plan documents. Therefore, plan fiduciaries must comply with the provisions of the IPS insofar as the policy directives or guidelines are consistent with the requirements of ERISA. Because of this, advisors should make sure the IPS's provisions are reasonably flexible, providing sufficient "wiggle room" about when and how any required investment course of action must be taken under the IPS.

IPS guidelines should also incorporate a review of the plan's investment fees. In recent years, plan fees have been attacked by the plaintiffs' bar, which has brought numerous legal claims against sponsors and providers. These suits generally allege that a lack of transparency and awareness contributed to the payment of excessive investment and recordkeeping fees by the plan and plan participants.

Excessive fees have become subject to heightened scrutiny by Congress, the DOL and the media. As a result of these concerns, it is a best practice to include guidelines in the IPS for evaluating the reasonableness of the fees and expenses charged by the plan's investment funds and recordkeeper and to adopt a formal Fee Policy Statement.

When commencing a new relationship with a plan client, an investment advisor should discuss the importance of the plan's IPS with the plan committee. Before recommending any changes to the plan's investments or investment menu, the advisor should verify that any new investment must the guidelines of the IPS.

When considering and approving any recommended changes to the IPS, it should be recalled that the act of changing the terms of the IPS may, in and of itself, be an exercise of fiduciary responsibility, and that the committee will be obligated to follow all of the terms of the IPS.

If the plan does not have an IPS or if the existing IPS is inconsistent with the plan's investment needs and objectives, the advisor should work with the committee to establish a new IPS.

Diversifying plan investments

It is critical to consider the "duty to diversify" under ERISA Section 404(a)(1)(C) whenever a plan committee selects plan investments. This duty requires the plan fiduciary to diversify the investments of the plan so as to minimize the risk of large losses, unless under the circumstances then prevailing it is clearly prudent not to do so. Note that this does not require that a fiduciary eliminate all risk or avoid all losses, but it is charged to "minimize the risk of large losses" to the plan. This principle recognizes that different asset classes perform differently at different times and that any investment may lose money. A properly diversified portfolio minimizes the risk that all adverse conditions will occur at the same time, resulting in large losses.

This duty has a special application to 401(k) plans, which by their nature divide investment responsibilities between the plan sponsor and the plan participants. The sponsor is responsible to maintain a proper menu of investment alternatives, and participants are responsible to make individual allocation decisions for their accounts. Naturally, the sponsor remains responsible for any investment losses that are the result of a flawed menu. For example, if a sponsor were to establish a limited menu of investment options in a narrow range of asset categories, making it impossible for participants to create a diversified portfolio, the sponsor would be in breach of its fiduciary duty to diversify.

[11] DOL Interpretive Bulletin 2016-01, Interpretive Bulletin Relating to the Exercise of Shareholder Rights and Written Statements of Investment Policy, Including Proxy Voting Policies or Guidelines, 29 CFR § 2509.2016-01.

[12] DOL Interpretive Bulletin 2016-01.

As a practical matter, the duty to diversify requires plan fiduciaries to ensure the plan's investment menu covers a sufficient number of asset classes and categories (e.g., cash and cash equivalents, large-cap and small-cap equities, fixed income securities). Even if the range of investments available through the plan's provider in certain asset categories is limited, plan fiduciaries should ensure that at least one investment option is included in the menu for each desired asset category. The plan menu should not have any impermissible gaps in its coverage of asset categories. Accordingly, fiduciaries should consider the full range of investments available to the plan through its provider in each desired asset category, including both actively managed funds and passively managed funds, ETFs and collective trusts.

Financial advisors should work with plan committees to determine whether a plan's investment portfolio — or in the case of a 401(k) plan, its investment menu — is sufficiently diversified. However, committees should be warned to avoid overreacting by concluding that the more investment options on a menu, the better.

Offering a very large number of investment options may actually confuse participants or may otherwise be counterproductive.

The trend has been to reduce the number of a plan's investment options; thus, making 10 to 20 investment alternatives available to participants is deemed to be sufficient to meet the diversification requirement. This range should be reflected in the plan's IPS.

Offering a broad range of investment alternatives

Section 404(c) of ERISA is the statutory provision that makes 401(k) plan participants solely responsible for their investment allocation decisions. A plan sponsor has no responsibility for investment losses resulting from a participant's allocation decision, but only to the extent the plan satisfies the conditions of ERISA Section 404(c). To be eligible for 404(c) protection, the plan must include "a broad range of investment alternatives" that is sufficient to provide participants with a reasonable opportunity to: (1) materially affect the potential investment return of their accounts, (2) choose from at least three alternatives with materially different risk and return characteristics, and (3) diversify the investments in their accounts so as to minimize the risk of large losses. Advisors should integrate the "broad range of investment alternatives" requirement into their advice when making recommendations about the number and range of investment options for a 401(k) plan menu.

In addition, in order to qualify for relief under Section 404(c), the plan generally must provide participants with an opportunity to exercise control over their accounts and to obtain sufficient information to make informed decisions regarding the plan's menu. The related 404(c) disclosure requirements are detailed and technical in nature. To meet the Section 404(c) requirements, many 401(k) plans include summary investment information in the enrollment kits for new participants (e.g., an investment brochure and fund fact cards). Prospectuses and summary prospectuses are also frequently included in these kits or mailed separately following the participant's initial investment in a fund. Participants must also receive an explanation that the plan is intended to constitute a Section 404(c) plan and that plan fiduciaries may be relieved of liability for plan losses as a result.

The prudence requirement

Each investment option on a 401(k) plan menu should be selected in accordance with the duty of prudence under ERISA, which requires a fiduciary to act "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." Courts have interpreted this duty as requiring plan fiduciaries to conduct an independent investigation of the merits of each of the plan's selected investments as seen in the context of the overall portfolio.[13] Accordingly, the essence of complying with this duty is following an investigative process for gathering relevant information and then considering such information when arriving at an investment decision.[14] If the committee lacks investment knowledge or experience, it would be consistent with its ERISA duties to engage an investment advisor to provide it with expert advice. While reliance on experts may be necessary, it does not serve to completely eliminate fiduciary responsibility; a fiduciary cannot be a mere "rubber stamp."

In the context of a 401(k) plan, the duty of prudence requires plan fiduciaries to ensure that each investment choice in the plan menu is a prudent investment option.[15] Appropriate consideration should be given to all relevant factors concerning a particular investment fund, including the role the investment fund will play in the plan's investment menu and a consideration of the risk of loss and the opportunity for gain.[16] Therefore, when recommending an investment fund for the plan menu, the advisor should also provide the committee with all relevant information concerning the fund, highlighting both the merits and possible drawbacks. By considering each fund's opportunity for gain and risk of loss, as well as all other relevant information, the sponsor will ensure its investment decisions are made prudently.

The test for prudence is procedural in nature, and it is not simply a question of how an investment fund performs once it has been selected. Plan committees should be made aware that ERISA's duty of prudence requires that they undertake an "investigative" process of information gathering before arriving at any investment decisions.

Considering investment fees

There has been an explosion in the number of fee-related lawsuits filed claiming that 401(k) plan sponsors imprudently selected funds with excessive fees or improper share classes and have paid excessive recordkeeping fees.

These excessive fee challenges are generally made in 401(k) plans or other defined contribution plans where there are participant-directed accounts. In the case of defined benefit plans, these charges cannot be made where the plan is fully funded. Even when the plan is not fully funded, these complaints are less frequently made.

[13] See, e.g., *Donovan v. Cunningham*, 716 F.2d. 1455 (5th Cir. 1983), cert. denied, 469 U.S. 1072 (1984).

[14] See also, e.g., In re Unisys Savings Plan Litigation, 74 F.3d. 420 (3d Cir.) cert. denied, 519 U.S. 810 (1996).

[15] Preamble to DOL regulations under ERISA Section 404(c), 57 Fed. Reg. 46922 (Oct. 13, 1992).

[16] See 29 C.F.R. 2550.404a-1(b)(1).

The early lawsuits set the template for many to follow.[17] The results of the entire body of litigation have been mixed, with many defendants ultimately settling for multiple millions of dollars and a few escaping on motions to dismiss. The common themes, however, include allegations that the plan committees failed to implement appropriate due diligence procedures, or had procedures but failed to adequately follow them, or that the plan failed to provide sufficient disclosures about fees and expenses so that participants could make sound investment choices for themselves. A committee's strongest protection is to meet regularly, follow a prudent process to exercise due diligence, provide full and fair disclosure, and keep a written record of its decision making.

Some of the lawsuits claimed that inadequately disclosed revenue sharing payments made from the plan's funds or fund managers to service providers are evidence of excessive compensation that has been inappropriately authorized by the plan fiduciary. In light of this risk, the advisor should provide the sponsor with comprehensive information concerning the fees charged by an investment fund, as well as disclosures concerning any revenue sharing payments made by the fund manager and any similar payments made by the fund (e.g., 12b-1 fees, shareholder servicing fees, sub-transfer agency fees) to the plan's service providers. This information is described in the 408(b)(2) disclosures and the prospectuses for the investments.

A committee may wish to benchmark providers' services to ascertain the prevailing investment fees for a comparable group of plans. The objective of benchmarking is to confirm whether the chosen provider's fee is within a range comparable services and is not an outlier. Before selecting a benchmarking service provider, the committee should seek clarification of how the benchmark group of plans is determined, the quality of the underlying data, the scope of plan services, and fees covered by the benchmarking analysis. The committee should also determine how the benchmarking results will be presented and explained.

Financial advisors can assist the committee in selecting a qualified provider of benchmarking services, and they can also help the committee evaluate the benchmarking results in their proper context. A committee should make investment decisions based on all relevant factors – and never based on an isolated review of fees or benchmarking results alone. If any portion of the plan's investment fees is used to pay for administrative services to the plan, the evaluation of the investment fees should also consider the quality of these services.

Monitoring investments

A fiduciary's duties do not end with prudently selecting a fund. Plan committees responsible for investment selection have a duty to monitor their plan's investments or investment menu choices at regular intervals to ensure that each investment remains prudent. Compliance with this duty of prudence requires proper documentation of the investment review process.[18] All investment reviews should follow the guidelines in the IPS, and any decisions resulting from this process should be put into writing. And just as the plan's menu is reviewed, the IPS itself should be reviewed on an ongoing basis and revised as necessary.

At each investment review meeting, the plan fiduciaries should confirm that the menu continues to provide a "broad range of investment alternatives" for ERISA purposes. It should evaluate the investment performance, volatility, style, fees and other relevant data for each investment fund. If the plan experiences a significant increase in the number of participants or growth in plan assets, the plan committee should pay particular attention to the continuing suitability of an investment fund's share class and the related 12b-1 fees and other expenses. It may find that the growth provides access to better priced funds or share classes that may be more prudent choices for the growing plan.

If during the review process the committee becomes dissatisfied with a particular investment option or finds that it no longer meets the guidelines of the IPS, the committee must decide if further action should or must be taken. One way of making this determination is by putting the challenged fund on a "watch list," which would typically require enhanced monitoring during a probationary period (e.g., reviewing performance more frequently and using investment analytics to dissect performance). If the fund does not improve or the committee otherwise decides to eliminate the investment, the challenged fund may be replaced by a new investment alternative.

[17] See e.g., *Hecker v Deere and Company,* cert denied 130 S.Ct. 1141 (2010), *Spano v. Boeing Company*, 633 F.3d 574 (7th Cir. 2011), *Will v. General Dynamics*, 2010 WL 4818174 (S. Dist. IL 2010).

[18] DOL Interpretive Bulletin 08-2; *Tibble v. Edison International*, 135 S. Ct. 1823 (2015).

RESOLVING
BENEFIT CLAIMS

The plan committee is ultimately responsible for resolving participant benefit claims through the plan appeals process whenever it acts as the plan Administrator. This is true even if the initial determination on benefits liability is handled by in-house staff or an outside vendor.

Only a plan fiduciary may exercise discretion about the administration of a plan so only the fiduciary committee may determine claims upon appeal. The terms of the plan document must be strictly followed during this process so it becomes important that at least one committee member has a working knowledge of the various benefit programs that might be reviewed. If a disputed benefit claim is presented on appeal, it is essential that the committee expeditiously affirm or reverse the initial benefit determination within the time limits set by the plan and the DOL's claim review procedures.

Mitigation of risk

Remember that a a fiduciary that breaches its responsibilities under ERISA is personally liable for any losses to the plan resulting from the breach and must disgorge related profits. Fiduciaries can also be subject to civil penalties for breaching their duties. A fiduciary might also be held responsible for the misconduct of co-fiduciaries and service providers.[19]

The committee should review the adequacy of the fidelity bond's coverage amount at regular intervals, but it should recognize that ERISA fidelity bonds are designed to protect the plan and not fiduciaries. Although it is not required to do so by law, a plan committee is well-advised to take steps to have fiduciary liability insurance coverage for all plan fiduciaries, including the committee's own members. It should periodically assess whether the coverage has sufficient limits and arrange for additional coverage if needed. Waiting until the last minute to investigate insurance coverage can be a costly mistake, since it is often too late to develop a strategy to minimize a plan fiduciary's potential exposure once a significant failure relating to a fiduciary breach occurs or is alleged.

Although a plan may not purchase fiduciary liability insurance for a fiduciary, the fiduciary itself or the plan sponsor may do so.[20] Purchasers of fiduciary liability insurance should ensure that their policy contains the appropriate coverages, including protection against liability for breaches of fiduciary duty, negligent advice regarding benefits eligibility, defense costs, punitive damages, civil penalties under ERISA, and sanctions imposed under DOL, PBGC and IRS compliance programs. Some insurers interpret exclusionary language in their policies very aggressively to their own advantage. Plan committees would do well to work with brokers who specialize in fiduciary coverage. These specialists can be attentive to when exclusions will be applied and what coverage gaps might be closed.

Furthermore, plan sponsors often indemnify fiduciaries who are employed for all actions or omissions done in reasonable good faith.

Conclusion

Plan committees are responsible to oversee a broad array of plan investment and administrative functions. In this role, they are acting in a fiduciary capacity, which requires them to implement processes that gather all the relevant information for each issue faced, which must then be evaluated to arrive at a reasoned and documented decision. This approach will result in effective plan governance that eliminates much of the fiduciary risk and ultimately facilitates the plan's delivery of benefits to its participants and beneficiaries.

Exhibit A is offered as a checklist for how a plan sponsor may assess its readiness for meeting these important responsibilities.

[19] ERISA Section 409.

[20] DOL Interpretive Bulletin 75-4, 29 CFR § 2509.75-4 states, "Indemnification provisions which leave the fiduciary fully responsible and liable, but merely permit another party to satisfy any liability incurred by the fiduciary in the same manner as insurance purchased under section 410(b)(3), are therefore not void under section 410(a)."

EXHIBIT A

Plan sponsor self-assessment and checklist		Yes	No
1 **Named Fiduciary and plan Administrator duties**	**Proper delegation of responsibilities** • If the plan sponsor has retained the title of Named Fiduciary or plan Administrator, have the duties of these fiduciary positions (e.g., investments, government reporting and participant disclosures) been properly delegated in writing to one or more plan committees? • If a Named Fiduciary or plan Administrator other than the sponsor will be appointed, has the appointment been made pursuant to the process described in the plan document?*		
2 **Structure and duties of plan committee**	**Committee charter** • Has a plan committee charter been adopted to delineate committee composition and duties? • Is committee membership limited to a workable number (e.g., 3 to 7 members)? • If term limits are used for committee membership, have the terms been staggered so as to retain institutional knowledge and continuity?		
3 **Plan committee meetings**	**Schedule and agenda for meetings and minutes** • Are plan committee meetings being held on a regular periodic basis? • Are meetings conducted pursuant to an agenda prepared and circulated in advance of the meeting that focuses on immediate and long-term goals? • Do outside consultants and experts attend committee meetings and respond to questions about agenda issues as well as report on new developments? • Are written minutes of plan committee meetings and deliberations being maintained?		
4 **Investment policy statement**	**Development and implementation of IPS** • Has the committee overseen the development of an investment policy statement (IPS) appropriate to the needs of the plan? • Is the IPS periodically reviewed and revised? • Are the committee's investment decisions being made in accordance with the guidelines set forth in the IPS?		
5 **ERISA Section 404(c) qualification**	**Range of investment options** • Is the range of plan investment options sufficiently broad to enable participant decisions to materially affect investment returns? • Do the investment options enable participants to diversify investments so as to minimize the risk of large losses? • Does the investment menu include at least three investment options from different points on the risk/return spectrum? • Are investment options limited to a number that will not overwhelm participants or result in dilution of the plan's bargaining power with investment providers?		
6 **Plan investment menu**	**Process for selecting investment options** • If committee members lack investment knowledge or experience, has the committee engaged an investment expert to provide advice? • Have all the relevant facts about a potential investment option (not just performance) been considered? • Has the committee considered each investment's fees and expenses? • Has the committee considered engaging benchmarking services to help evaluate investment performance as well as fees and expenses?		
7 **Ongoing investment reviews**	**Monitoring** • Is the committee reviewing the performance of investment options on the plan investment menu at regular periodic intervals and at least annually? • Do the committee's reviews include fees of investment and service providers? • Is indirect compensation to investment and service providers being monitored? • If an investment is put on a watch list, does the committee follow through by removing the investment from the plan menu if it does not improve?		
8 **Review of benefit decisions**	**Appeals of benefit denials** • Do committee members have a working knowledge of plan benefits and the terms for benefit eligibility? • Are participant appeals being handled expeditiously and without unusual delays?		

* A well-drafted plan document provides: (1) how the committee members are appointed, or (2) that they shall be appointed pursuant to the committee charter.

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About Marcia Wagner and The Wagner Law Group

Marcia Wagner is the founder of The Wagner Law Group, one of the nation's largest and most highly regarded law firms specializing in ERISA, employee benefits and executive compensation, and has practiced employee benefits law for over 30 years.

She is an authority on qualified and non-qualified plans, fiduciary issues, deferred compensation, and welfare benefit arrangements, with experience in plan design and drafting, compliance, tax planning and consultation on all aspects of ERISA and the Internal Revenue Code. Ms. Wagner also serves as an expert witness in ERISA litigation.

Ms. Wagner specializes in Title I of ERISA, and has obtained advisory opinions, information letters and prohibited transaction exemptions from the DOL. She handles fiduciary matters impacting plan sponsors, investment and other fiduciary committees, investment managers and advisors, recordkeepers, broker-dealers, banks, and other financial services firms. Ms. Wagner advises clients on the avoidance and rectification of prohibited transactions, the development of compliance programs, and investment policies. She is a renowned expert in issues concerning pension plan investments and fiduciary issues, and her opinion has been sought by noted authorities in the employee benefits area, including governmental agencies.

She was appointed Chair of the Employee Plans subcommittee of the IRS Tax Exempt & Government Entities Advisory Committee and received that agency's highest honor. She is a Fellow of the American College of Employee Benefits Counsel and is the recipient of more than 50 professional honors.

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