



# Understanding your fiduciary role

A plan sponsor fiduciary guide

## ABOUT

Perhaps no one topic in the employee benefits arena has drawn more attention and scrutiny over the last several years than the role of the plan fiduciary and the responsibilities fiduciaries have to the plan and its participants. Of particular note has been the fiduciary's role with respect to plan investments.

Is it enough for the plan fiduciary to simply select various investment options and make them available to the plan? What exactly is a plan fiduciary? How about ERISA §404(c) protection? What is it and how will it help your company?

This fiduciary guide can help you understand and manage your fiduciary responsibilities through a better understanding of existing rules and regulations. In addition, the information in this guide can help you monitor your procedures, as well as document your decisions.

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This guide is not meant to provide legal advice and is not intended to be a comprehensive review of all matters related to fiduciary responsibilities. As with all matters pertaining to your plan, you should consult with your legal counsel for expert assistance.

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# The role of a fiduciary

**WHAT IS ERISA?** ERISA is the acronym for the Employee Retirement Income Security Act, a federal law enacted in 1974. ERISA regulates employer-sponsored retirement and welfare benefit plans. One of the primary purposes of the act is to impose specific duties on plan fiduciaries.

## WHAT ROLE DOES THE DEPARTMENT OF LABOR (DOL) PLAY?

It is the responsibility of the U.S. DOL to enforce ERISA. In some ways, the DOL has similar responsibilities to those of a plan fiduciary; it keeps a close eye on employers to ensure that plan participants' best interests are adequately served.

## WHAT ARE THE MAIN RESPONSIBILITIES OF A FIDUCIARY?

ERISA imposes specific duties upon plan fiduciaries, including:

- **Duty of loyalty:** Known as the “exclusive benefit rule,” it states that a fiduciary must perform his or her duties solely in the interest of participants and beneficiaries, for the exclusive purpose of:
  - Providing benefits to participants and beneficiaries, and
  - Defraying reasonable expenses of administering the plan
- **Duty to act prudently:** Interpreted by the courts to be a “prudent expert” rule, it states that a fiduciary must act with the “care, skill, prudence, and diligence ... that a prudent man acting in a like capacity and familiar with such matters would use ...” [ERISA §404(a)(1)(B)]
  - Fiduciaries may need to hire or consult with an expert if they do not have the expertise on their own.
  - Acting in good faith is not sufficient.
  - A prudent decision-making process can be more important than the outcome of a decision.
  - Decisions and meetings should be properly documented.
- **Duty to diversify investments:** A fiduciary should act to diversify investments so as to minimize the risk of large losses, unless, under the circumstances, it is clearly prudent not to do so.
  - Diversification is measured with respect to the plan's entire assets, not at the level of the individual manager or investment option.
  - This is one requirement for ERISA §404(c) protection (discussed on page 5).

- **Duty to follow plan provisions:** To the extent not inconsistent with ERISA, fiduciaries must follow the terms of the governing documents for the plan.
  - The plan document provisions should be periodically reviewed and kept up-to-date.
  - Other plan-related documents (e.g., the investment policy statement) should also be considered when carrying out this duty.
  - Consistency across plan-related documents is important.

## HOW DO I KNOW IF I AM A PLAN FIDUCIARY?

In general, you are a “plan fiduciary” if you:

- Have any discretionary authority or discretionary responsibility in the administration of the plan
- Exercise any authority and/or control over the management or disposition of plan assets
- Render investment advice to the plan and/or its participants for a fee or other compensation, whether direct or indirect

Certain roles are typically fiduciary in nature:

- Plan sponsor
- Plan trustee
- Plan administrator
- Administrative and investment committees
- Investment manager

## MANY PEOPLE IN MY OFFICE HELP ADMINISTER THE PLAN. ARE THEY ALL CONSIDERED PLAN FIDUCIARIES?

It is equally important to know who is and who is not a fiduciary. In general, a person who performs certain ministerial administrative functions within a framework of the plan’s policies, practices and procedures is not a fiduciary.

Ministerial administrative functions may be fulfilled by the following:

- Directed trustee
- Recordkeeper
- Attorney
- Accountant
- Actuary
- Third-party administrator
- In-house benefits analyst

## CAN A PERSON BE HELD PERSONALLY LIABLE FOR NOT FULFILLING HIS OR HER FIDUCIARY OBLIGATIONS?

ERISA §409 provides that “any person who is a fiduciary with respect to a plan who breaches any of the responsibilities, obligations or duties imposed upon fiduciaries by this subchapter shall be personally liable to make good to such plan any losses to the plan resulting from each such breach ...”

## HOW CAN A FIDUCIARY LIMIT THE RISK?

Fiduciary risk is often more about following stated processes and procedures than about the actions taken.

Know what the DOL would look for in an audit:

- Written policies and procedures
- Documentation of decisions made, and other evidence that policies and procedures are being followed
- Compliance with ERISA §404(c) to the extent that the plan has declared itself to be a §404(c) plan
- The appropriate level of coverage in an ERISA fidelity bond (see following page)

Plan sponsors should consider indemnifying fiduciaries for lawsuits that may arise under ERISA. Another avenue to protect the personal assets of fiduciaries from ERISA claims is to purchase fiduciary liability insurance, although this is not required under ERISA.

## What is an ERISA fidelity bond?

ERISA §412(a) requires that each plan fiduciary and every person who handles plan assets (including funds and other property of the plan) maintain a fidelity bond. The required ERISA fidelity bond protects the plan from loss of property resulting directly from dishonest or fraudulent acts of those covered by the bond. The amount of the bond must be at least 10% of the value of the funds handled (minimum of \$1,000 per plan) and generally need not be greater than \$500,000 per plan. For plans that hold employer securities, the maximum bond amount that can be required for any one plan official is \$1 million.

For additional information on Fiduciary Standards of Conduct, you may also log on to <http://www.dol.gov/ebsa/fiduciaryeducation.html>.

## ERISA §404(C)

Plan fiduciaries have the primary responsibility for the operation and administration of a plan. This includes the selection and monitoring of the plan's investments, taking into account the fiduciary duties described earlier. It also means that fiduciaries can be held liable for investment decisions made by participants, but ERISA §404(c) provides relief from this liability. For participants who exercise control over their plan investments, §404(c) generally shifts the responsibility for the resulting investment returns from the fiduciary to the participant.

While compliance with §404(c) is voluntary, most fiduciaries of defined contribution plans (for example, 401(k) plans) try to take advantage of this important protection. There are very specific requirements that must be satisfied to comply with §404(c). Plan sponsors should:

- Notify participants that the plan intends to comply with ERISA §404(c), and that fiduciaries may be relieved of losses resulting from participants' investment instructions (this critical step cannot be overlooked)
- Offer a broad range of investment options (at least three diversified alternatives with different risk and return characteristics are a minimum)
- Provide participants with sufficient investment information to make informed decisions, including the fee and investment information (participant fee disclosure) required by ERISA §404(a):
  - Some information must be provided automatically upon initial eligibility, and annually thereafter
  - Other information must be provided upon request

- Provide participants with the information and ability to select among available investments, including the ability to transfer among funds on a frequency based on the volatility of the investments (but no less frequently than quarterly)
- Provide written confirmation to participants of their investment instructions

If an available investment option includes employer securities (company stock), additional requirements apply:

- Voting and other shareholder rights must be passed through to participants.
- Procedures must be in place to protect the confidentiality of participant holdings and transactions in stock, and the fiduciary responsible for monitoring compliance must be identified.

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Despite §404(c),  
fiduciaries are still  
responsible for the  
ongoing monitoring and  
selection of available  
investment options.

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This is not an exhaustive list of requirements for compliance with §404(c). Consult with your legal advisor for further information.

# QDIA: What you need to know

**GENERALLY, PLAN FIDUCIARIES DO NOT RECEIVE §404(C) PROTECTION WHEN PARTICIPANTS FAIL TO MAKE INVESTMENT DECISIONS AND THUS ARE DEFAULTED INTO AN INVESTMENT SELECTED BY THE FIDUCIARIES.** However, there is an exception. A qualified default investment alternative (QDIA) provides limited fiduciary protection in participant-directed defined contribution plans that default participants into this investment. The QDIA is a default investment that meets certain criteria set forth in the DOL regulation. A QDIA must be an investment or model portfolio that is diversified to minimize the risk of large losses. In addition, it is designed to provide varying degrees of long-term appreciation and capital preservation through a mix of equity and fixed income investments. In general, there are three standard categories of QDIAs available:

- **Age-based or target date fund:** The asset allocation is based on the participant's age, target retirement date or life expectancy. Such investments or portfolios must change their asset allocations and associated risk levels over time, with the objective of becoming more conservative (i.e., decreasing risk of losses through higher allocation to fixed income investments) as the participants age.
- **Balanced fund:** The asset allocation is based on characteristics appropriate for the group of employees as a whole, rather than the age, risk tolerances or other preferences of any individual participant.
- **Managed account:** This is an investment service in which the asset allocation is created using existing plan investment options and which takes into account the individual's age, target retirement date or life expectancy. This allocation and associated risk level must change over time, with the objective of becoming more conservative (i.e., decreasing risk of losses through higher allocation to fixed income investments) as the participants age.

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A special type of QDIA is allowed only in conjunction with an eligible automatic enrollment arrangement that allows participants to request a refund of deferrals made soon after being automatically enrolled in the plan. This QDIA is designed to preserve principal and is only allowed for up to 120 days after a participant's first elective default contribution.



## HOW CAN I SATISFY THE REGULATION?

A plan fiduciary who complies with the regulation is relieved from certain fiduciary liability for investing participant assets in a default investment in situations in which a participant did not provide investment direction. Below is a partial list of conditions that must be satisfied to comply with the regulation:

- Assets must be invested in a QDIA.
- Participants must have had an opportunity to provide investment direction, but failed to do so.
- A QDIA notice generally must be furnished to participants at least 30 days prior to the first investment in the QDIA and prior to each plan year thereafter.
- Material describing the QDIA must be furnished to participants.
- Participants must be able to direct investments out of the QDIA as frequently as participants who affirmatively invested in the QDIA, but no less frequently than once within a three-month period.
- Transfer fees or restrictions cannot be imposed upon a defaulted participant who transfers out of the QDIA within 90 days of the first investment. After the 90-day period, the default investment may be subject to the same transfer fees and restrictions that apply to all participants.
- The plan must offer a wide range of investment alternatives as defined in the §404(c) regulations.

# Qualified change in investment options (QCIO)

## **UNDOUBTEDLY, THERE WILL COME A TIME WHEN PLAN FIDUCIARIES DECIDE TO MAKE A CHANGE TO ONE OR MORE INVESTMENT OPTIONS IN A DEFINED CONTRIBUTION PLAN.**

When changes occur, a decision needs to be made with respect to the assets held in any fund that is being eliminated. It is common practice for assets held in the eliminated fund(s) to be transferred directly (“mapped”) to the replacement fund(s). Recall that §404(c) provides protection to fiduciaries only for investment directions given by participants. The decision to “map” and the mapping strategy employed are determined by the plan’s fiduciaries, rather than decided by the participants. Therefore, fiduciaries generally bear the risk for investing the assets in the replacement fund(s).

There is, however, an important exception. If the change constitutes a qualified change in investment options (QCIO), fiduciaries receive protection under §404(c) for the mapping of assets. Among the requirements of a QCIO:

- Participant accounts must be reinvested among one or more new investment options when participants fail to provide contrary investment instructions in advance of the change.
- Affected participants’ accounts immediately before the change were invested at the direction of those participants (i.e., QCIO protection does not apply if participants were defaulted into their prior investments for lack of providing investment direction).
- The characteristics of the new investment option(s), including risk and rate of return, are reasonably similar to those of the eliminated fund(s).
- Notice is provided to affected participants 30 to 60 days prior to the change.

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Recall that §404(c) provides protection to fiduciaries only for investment directions given by participants.

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The notice must contain the following information:

- A description of the change
- Information comparing the option(s) being eliminated with the new investment option(s)
- An explanation that unless an affirmative investment election is received, balances in the replaced option(s) will be invested in the new option(s)

No formal guidance has been provided to assist plan fiduciaries in determining if replacement funds being mapped are similar to the replaced funds for purposes of QCIO protection. Therefore, it may be appropriate to engage investment professionals when making this determination.

## A WORD ABOUT EXPENSES

Under ERISA §408(b)(2), fees and expenses paid to service providers for the administration and ongoing maintenance of a plan must be reasonable when considering the value of such services. A question often arises as to what plan-related fees or expenses can appropriately be paid from plan assets. Fees are generally related to either settlor activities or fiduciary activities. Only those reasonable fees related to fiduciary activities are permitted to be paid from plan assets, and then only if the plan document so stipulates.

Settlor activities are those that confer a benefit upon the plan sponsor. Fees for these activities cannot be paid from plan assets. Examples of settlor activities and functions include:

- The establishment or termination of a plan
- Plan design studies and union negotiations related to plan design
- Discretionary amendments to a plan, including those related to a plan design feature

- The determination of plan liability and expenses for financial accounting purposes

Fiduciary activities relate to the proper administration of a plan in accordance with applicable law and the plan's provisions. Examples of fiduciary activities (the fees for which can generally be paid from plan assets) include:

- Recordkeeping and other plan administrative activities
- Annual plan audit and completion of required government filings (e.g., Form 5500)
- Drafting of legally required amendments needed to maintain the tax-qualified status of the plan
- Actuarial valuations and Pension Benefit Guaranty Corporation (PBGC) premiums for a defined benefit plan

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This is not intended to be a comprehensive list of activities. As some activities may have components of both settlor and fiduciary functions, legal counsel should be sought before an expense is paid from plan assets.

# Establishing a plan committee

**IDENTIFY THE RIGHT PEOPLE FOR YOUR PLAN COMMITTEE.** Your committee should include individuals with backgrounds useful to plan administration, finance and investments, as well as individuals experienced in implementing decisions and processes within the company. You may want to consider establishing separate committees for plan administration and plan investments, as they require different skills. Consider appointing fiduciaries by title, and determine if it is appropriate to give the company's board of directors a fiduciary role. Be sure to educate committee members about their duties, and make sure they understand the hat they wear and when they wear it.

## DEFINE FIDUCIARY RESPONSIBILITIES

Clearly assign duties among committees and fiduciaries, and if the company's board of directors has a role, define it. One of your named fiduciaries may select other named fiduciaries or delegate duties to someone not specifically named as a fiduciary to fulfill certain responsibilities. The key to successful delegation is to ensure that all those charged with fulfilling these duties understand the importance of their role.

The appropriate retirement plan committee or named fiduciary may be responsible for appointing recordkeepers, investment advisors, trustees and other plan service providers. A committee also may want to engage appropriate advisors to educate the committee on investments or other matters. While these professionals can provide valuable assistance to the plan fiduciaries, the selection and monitoring of the service providers are themselves fiduciary responsibilities. When evaluating these providers, the plan fiduciaries will want to consider the qualifications of the providers, the quality of the services given and whether the total direct and indirect fees paid by the plan for those services are reasonable in light of the services provided.

## ESTABLISH, DOCUMENT AND REVIEW PROCESSES AND PROCEDURES

Regular committee meetings should be held and special meetings called when circumstances require it. A written agenda should be circulated in advance of meetings, so that committee members can properly prepare to discuss the topic(s) at hand and make appropriate decisions.

The focus should be on establishing prudent processes and controls for committees to follow. This is called “procedural prudence” and is effective in managing fiduciary liability. The courts often look more closely at the process than the results of decisions. Keep detailed meeting minutes to document how and why decisions were made (or not made). If decisions were based on consultation from outside experts, incorporate that input into meeting minutes as appropriate.

## SPECIAL CONSIDERATIONS FOR INVESTMENT COMMITTEES

Fiduciaries are responsible for the selection and monitoring of the plan’s investments. This is true even for a defined contribution plan that complies with ERISA §404(c) to shelter fiduciaries from liability for losses resulting from a participant’s investment direction. Consistent with the theme of procedural prudence, a properly drafted investment policy statement (IPS) can go a long way in helping fiduciaries fulfill their duties.

The IPS reflects the plan’s specific goals and objectives. In general, an IPS should outline five main objectives: the intended purpose of the plan, its long-range investment framework, an outline of the investment selection process, a monitoring and replacement process, and a clear definition of related investment duties and responsibilities.

## WHAT ARE THE BENEFITS OF AN IPS?

There are several advantages in creating an IPS, not the least of which is that it helps document the approach to be used in the selection of the investments for your plan. Benefits of an IPS include:

- **Documentation:** An IPS provides for written documentation as to the policies, practices and procedures for making investment selections.
- **Clarification:** Your business is like many other businesses in that the individual(s) responsible for plan administration may come and go. An IPS provides a clear baseline and framework to ensure continuity in its adherence and helps negate “second-guessing.”

- **Communication:** When there is an IPS, participants can be assured that there is a logical and disciplined approach to the process.
- **Protection:** Establishing an IPS can serve as an important line of defense against potential fiduciary liability.

## WHO IS RESPONSIBLE FOR DRAFTING THE IPS?

Like all fiduciary documents, an IPS should be carefully drafted and thoroughly reviewed by the plan sponsor and the plan’s advisors and/or consultants. An IPS can take many forms and can be rather extensive.

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Be sure to educate committee members about their duties, and make sure they understand the hat they wear and when they wear it.

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# ERISA quick compliance checklist

Compliance with ERISA begins with knowing the rules. Plan administrators and other plan officials can use this checklist as a quick diagnostic tool to begin assessing a plan's compliance, but remember it is not a substitute for a comprehensive compliance review.

If you answer “**No**” to any of the following questions, your plan may be at risk of not complying with ERISA's requirements.

## Questions

Yes No

### Processes and procedures

Are plan fiduciaries educated with respect to their duties and obligations?

Do plan fiduciaries meet regularly and keep well-documented minutes of those meetings?

Is there a prudent fiduciary decision-making process, and is there sufficient documentation to support actions taken?

Are the service provider arrangements reasonable, and is the cost and quality of those services in line with industry norms for the value received per ERISA §408(b)(2)?

Is your plan covered by a fidelity bond against losses due to fraud and dishonesty?

Did the plan obtain exemptions from the DOL for any financial transactions with persons related to the plan or any plan official (for example, if the plan made a loan to, or participated in an investment with, the employer)?

### Administration

Does the plan operate in accordance with applicable documents, statutes and regulatory requirements?

Does the employer or other plan sponsor remit participant contributions to the plan or trust on a timely basis?

Does the plan pay participants' benefits on time and in the correct amounts?

Were expenses paid from plan assets authorized in the plan document necessary for the proper administration of the plan and reasonable in amount?

Are all reporting and disclosure requirements being met (e.g., Form 5500)?

Are required notices and other communications sent to participants timely?

Have you provided plan participants with a summary plan description, summary annual report (annual funding notice for defined benefit plans), enrollment materials and summaries of any material modifications of the plan?

Do you respond to written participant inquiries for copies of plan documents and information within 30 days?

Do you maintain copies of plan documents at the principal office of the plan administrator for examination by participants and beneficiaries?

Does the plan provide and track ongoing employee communications and investment education?

### Investment related

Does your plan have a written investment policy statement or funding policy? If so, is it followed?

Has a plan fiduciary determined that the investments (and their associated risks) are prudent and solely in the interest of the plan's participants and beneficiaries?

Are the plan's investments diversified to minimize the risk of large losses? Or, if the plan permits participants to select investments, does the plan offer diversified investment options?

If participants are permitted to select their investments, has the plan provided them with enough information to make informed decisions, including required fee disclosures?

Do plan fiduciaries periodically monitor plan investments and prudently evaluate whether to keep or replace them, and maintain adequate documentation of their reviews?

Are the plan's investments compared with appropriate benchmarks and peer groups over varying periods of time?

## A few reminders

- Consult legal and/or outside plan experts about questions related to fiduciary responsibilities.
- Consider taking advantage of the various methods that may limit fiduciary liability or help mitigate risk.
- Keep in mind that a fiduciary's commitment is ongoing.
- Fiduciary standards require appropriate action, not a guarantee of results.

### Additional resources for fiduciary information

- U.S. Department of Labor—Employee Benefits Security Administration:  
[www.dol.gov/ebsa](http://www.dol.gov/ebsa)
- Plan Sponsor Council of America:  
[www.pasca.org](http://www.pasca.org)
- PLANSPONSOR:  
[www.plansponsor.com](http://www.plansponsor.com) (free registration required)
- Foundation for Fiduciary Studies:  
[www.fi360.com](http://www.fi360.com)
- Benefits Link:  
[www.benefitslink.com](http://www.benefitslink.com)
- 401(k) Help Center:  
[www.401khelpcenter.com](http://www.401khelpcenter.com)



TO LEARN MORE ABOUT HOW WE CAN SUPPORT YOU  
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**TARGET DATE FUNDS:** Target date funds are funds with the target date being the approximate date when investors plan to start withdrawing their money. Generally, the asset allocation of each fund will change on an annual basis, with the asset allocation becoming more conservative as the fund nears the target retirement date. The principal value of the fund(s) is not guaranteed at any time, including at the target date.

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