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FiduciarySource® Guide

Helping plan sponsors understand their fiduciary duties

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Introduction to the T. Rowe Price Fiduciary Guide

Fiduciary duties and responsibilities are a growing responsibility for workplace retirement plan sponsors. To help you meet these challenges, T. Rowe Price is committed to providing high quality education that reflects the latest and best thinking in this area. Through its **FiduciarySource**® program, T. Rowe Price offers our Fiduciary Guide to plan sponsors. This valuable resource provides a basic overview of fiduciary responsibilities applicable under the Employee Retirement Income Security Act of 1974 ("ERISA").

This guide is an introductory fiduciary resource for defined contribution retirement plan sponsors and their employees working with the plan(s). It streamlines complex fiduciary topics into an easy-to-understand format. The goal is to help plan sponsors determine who their plan's fiduciaries are, and what basic duties those fiduciaries have. This material can help lay the foundation for the development of good fiduciary practices, such as asking the right questions, creating a process for decision making, and seeking help from experts when needed.

The emphasis is on providing general principles, not specific formulas. Readers should recognize that there is no "one-size-fits-all" when it comes to fiduciary best practices. What may be appropriate for a large retirement plan sponsor may be very different when compared to a retirement plan sponsored by a small business with fewer resources.

This guide can't tell you everything you will ever need to know about being a fiduciary, and it can't take the place of legal advice regarding what to do in a particular situation. You should seek counsel for specific issues as you encounter them.

To provide the best thinking from diverse perspectives, each chapter of our Fiduciary Guide has been authored by an ERISA expert with distinct points of view and extensive experience representing plan sponsors and educating them on their responsibilities.

If you are already familiar with the basics of "who" and "what" in relation to fiduciary responsibility, but you have a special interest in a particular topic (e.g., litigation), the material is designed so you can turn directly to chapters and selected topics.

We sincerely hope you find this resource helpful as you scratch the surface of a complex but increasingly important responsibility—a responsibility which is designed to help safeguard the retirement security of you and your co-workers.

Margaret H. Raymond, Esquire
Managing Counsel,
T. Rowe Price Retirement Plan Services, Inc.

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MY ROLE AS A FIDUCIARY

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Before you read further, determine whether you or someone else in your organization is a fiduciary. That's important because fiduciaries have important responsibilities in protecting retirement benefits. **In this chapter, we will help you identify who is a fiduciary, distinguish fiduciary from non-fiduciary activities, and better understand permissible delegation of fiduciary responsibilities to another individual.**

Who is a fiduciary?

Many individuals involved in running the company 401(k) or other retirement plan are not fiduciaries under ERISA, such as the people who handle the day-to-day activities but do not exercise discretion. The plan fiduciaries are those who make, or have the authority to make, the decisions on behalf of the plan.

In general, a fiduciary is an individual or entity (such as a plan fiduciary committee or the sponsoring employer's board of directors) who:

- Exercises *discretionary authority* or control over the management of a plan or over the management or disposition of its assets;
- Provides *investment advice for a fee* (typically an outside investment advisor); or
- Has any *discretionary authority* or *responsibility* in the administration of such plan.

A key word in ERISA's fiduciary definition is "discretionary." That is, a person (an individual or entity) responsible for overseeing a plan's operation will generally be considered a fiduciary only to the extent the person applies discretionary authority or control over plan management or plan administration.

It is important to understand that ERISA's "fiduciary" definition generally is "functional"—meaning the functions a person actually performs with respect to a plan, not the person's title, will determine whether that person is a fiduciary. Thus, in determining whether a person is an ERISA fiduciary, it is irrelevant whether the person:

- Intends to act as a fiduciary;
- Knows that he or she is acting as a fiduciary; or
- Is authorized to act as a fiduciary.

> A person will generally be considered a fiduciary only to the extent the person applies discretionary authority or control over plan management or administration.

Although a person's fiduciary status under ERISA is generally determined based on the person's function rather than title, persons holding the following roles will automatically be considered fiduciaries:

- **Plan Administrator:** ERISA requires that a "plan administrator" be designated under the plan. The plan administrator is responsible for managing the day to day operation of the plan. These duties are set by ERISA and the terms of the plan. The plan administrator could be an individual, a committee, or the plan's sponsoring employer.
- **Trustee:** The plan's trustee has exclusive authority to manage and control plan assets. Many plans use a so-called "directed" trustee, some or all of whose duties are subject to the direction of a fiduciary who is not the trustee. The scope of a directed trustee's fiduciary responsibilities is limited to any undirected, discretionary authority over the management and control of plan assets.
- **Named Fiduciary:** ERISA requires the plan document to provide for one or more "*named fiduciaries*" that jointly or severally have authority to control and manage the operation and administration of the plan. Plans often specify a single "named fiduciary," such as a retirement committee, but the plan document can specify more than one named fiduciary and allocate fiduciary responsibilities among them. For example, it is common for a plan document to specify two committees as "named fiduciaries," one committee to be responsible for selecting and monitoring plan investments, and another committee to be responsible for overseeing all other plan administration and compliance activities.

It is critically important to understand which plan-related activities are "fiduciary" activities and which are not. In fiduciary litigation under ERISA, courts will identify fiduciary activities and the fiduciaries who perform them, and determine whether the fiduciaries' performance of those activities meets ERISA's strict fiduciary standards.

Fiduciary activities should be distinguished from "non-fiduciary" activities, which are often referred to as either "ministerial" or "settlor" activities. ERISA's fiduciary standards do not apply to non-fiduciary ministerial or settlor activities.

MINISTERIAL ACTIVITIES

Unlike fiduciary activities, where judgement or deliberation informs the discretionary exercise of authority or control over plan management or administration, non-fiduciary ministerial activities are performed on a non-discretionary basis pursuant to standards set by plan fiduciaries and the plan's governing documents. For example, an HR or benefits office staff employee who administers a 401(k) plan's loan or hardship withdrawal procedures in accordance with the governing terms of the plan document and applicable written administrative procedures (without the need to make discretionary determinations) will likely be performing non-fiduciary ministerial activities with respect to the plan, as long as the plan and procedures are clear.

SETTLOR ACTIVITIES

In general, a "settlor" establishes the plan and, if applicable, the plan's underlying trust or other funding vehicle. In the employee benefit plan context, the "settlor" is the plan sponsor, for example, the employer whose eligible employees participate in the plan. In general, non-fiduciary "settlor" activities are the activities relating to plan design or employer costs for the plan, including establishing, modifying, or terminating a plan.

Below are some examples of fiduciary activities and non-fiduciary “ministerial” and “settlor” activities:

EXAMPLES OF FIDUCIARY ACTIVITIES

- Selecting plan fiduciaries
- Selecting plan service providers
- Monitoring fiduciaries and outside service providers
- Providing investment advice for a fee
- Selecting plan investment options
- Monitoring plan investment options
- Interpreting plan provisions
- Exercising discretion in approving or denying benefit claims or appeals

EXAMPLES OF NON-FIDUCIARY ACTIVITIES

Ministerial Activities

- Applying rules to determine eligibility for plan participation or benefits
- Preparing employee communications
- Preparing required governmental reports
- Calculating benefits
- Educating participants about their rights and responsibilities under the plan
- Processing claims for benefits
- implementing participant investment elections

Settlor Activities

- Establishing a plan
- Adopting an amendment to a plan
- Approving the termination of a plan
- Conducting a study of the plan’s design or its financial impact upon the plan sponsor

ACCIDENTAL FIDUCIARY

An individual who is responsible for administering a plan but who is not intended to be a plan fiduciary should be careful not to become an “accidental fiduciary.” For example, an individual whose responsibilities include only ministerial activities such as administering the plan’s participant loan program could unwittingly become an accidental fiduciary by exercising discretion and interpreting the loan provisions of the plan document or the plan’s written loan procedures. An individual who becomes an accidental fiduciary is in a very vulnerable position, especially if the individual is not reimbursed by the plan sponsor or covered by the plan sponsor’s fiduciary liability insurance policy. The best protection is to not become an accidental fiduciary in the first place. The next-best protection is for anyone who becomes an accidental fiduciary to be indemnified or covered by a fiduciary liability insurance policy.

PLAN GOVERNANCE, DELEGATION OF FIDUCIARY DUTIES & DUTY TO MONITOR

There is no "one-size-fits-all" prescribed structure under ERISA that a plan sponsor must establish to govern its benefit plan(s). Plan governance structures vary, depending upon the size and culture of the plan sponsor, the type of plan, and other factors. However, given the current legal environment and potential for ERISA fiduciary liability, formalized plan governance structures are becoming more common.

For example, it has become more common for plan sponsors, acting through their boards of directors or other governing bodies, to appoint fiduciary committee(s) to oversee plan investments and operations. Smaller plan sponsors sometimes appoint an individual fiduciary rather than a fiduciary committee to oversee some or all plan management activities. When the plan sponsor's board of directors or other governing body appoints an individual fiduciary, a fiduciary committee or other named fiduciary, it will assign specific fiduciary duties to that fiduciary.

It is advisable that the specific fiduciary responsibilities are clearly described in the appointing resolutions and in the plan document. If a fiduciary committee has been appointed, it is also good practice for the committee's charter to include, among other things, a description of the committee's responsibilities that are consistent with the plan document and appointing resolutions. It is also advisable that the plan governance documents specify the extent to which a fiduciary committee or other named fiduciary may delegate its duties. Unless restricted, the fiduciary committee or other named fiduciary may then delegate some of its duties, for example, to an HR or benefits office staff employee, a subcommittee, or an outside service provider. Of course, any undelegated activities would be retained by the fiduciary committee or other named fiduciary.

Although a fiduciary committee or other named fiduciary may be permitted to delegate its duties to an employee, a subcommittee or an outside service provider, the fiduciary committee or other named fiduciary will continue to be responsible for monitoring the delegate's performance of the delegated duties. This is because delegation and monitoring are both fiduciary activities under ERISA.

> Although a fiduciary may be permitted to delegate its responsibilities, the fiduciary will continue to be responsible for monitoring the delegate's performance of the delegated responsibilities.

Given the regulatory complexities and administrative burdens involved in maintaining a retirement plan, plan sponsors often outsource certain administrative activities to one or more external service providers, such as:

- 401(k) recordkeeping;
- Approval and/or processing of:
  - QDROs;
  - Loans; and/or
  - Hardship withdrawals;
- Investment advisory services;
- Custodial services; and
- Claims administration.

When outsourcing administrative activities, it is very important to understand the scope of the external service provider's duties and whether those duties include fiduciary duties. It is not always clear whether an external service provider has taken on fiduciary duties. Here are two examples:

- **Hardship Withdrawals:** If the external service provider has been engaged to approve and process hardship withdrawal requests, and the approval process requires the external provider's discretionary determination of whether a "financial hardship" exists, then the service provider will be considered a fiduciary. On the other hand, if the plan document's hardship withdrawal provisions permit withdrawals only for the so-called "safe harbor" financial hardship reasons, the service provider arguably will be acting only in a non-fiduciary, ministerial capacity when it determines whether any of the safe harbor reasons are present.
- **QDROs:** Determining whether domestic relations orders qualify as QDROs is a fiduciary function because it involves discretionary authority or control over the management of a plan and/or disposition of its assets. If the external service provider has been engaged to approve and administer QDROs, it will be important to understand whether the service provider has been given full responsibility to make the final QDRO determination (in which case, the service provider will be a fiduciary), or whether the appointing fiduciary has retained that responsibility (in which case, the service provider will not be a fiduciary).

Regardless of whether an external service provider is a plan fiduciary, the appointing fiduciary retains the fiduciary duty to monitor the service provider's performance.

UNDERSTANDING THE ALLOCATION OF RESPONSIBILITIES

It is important for all parties involved in the management and administration of an ERISA employee benefit plan—be they plan sponsors, fiduciary committees, employees of the plan sponsor, or outside service providers—to understand not only every activity related to plan management and administration, but also which party is responsible for performing each activity. If there is confusion as to who is responsible for what, it's helpful to review plan documents, committee charters, resolutions, and other plan governance documents, and to develop a comprehensive list of all plan management and administration activities that distinguishes fiduciary from non-fiduciary activities.

Anyone who has any responsibility with respect to an ERISA employee benefit plan should understand whether he or she is an ERISA "fiduciary" and whether any of the plan-related activities he or she is responsible for performing are ERISA fiduciary activities. These are fundamental issues that will affect not only how the responsible party carries out his or her plan-related duties, but also whether that party needs to be protected by fiduciary liability insurance or indemnification.

> Anyone with responsibility with respect to an ERISA employee benefit plan should understand whether he or she is an ERISA "fiduciary" and whether any of the plan-related activities he or she is responsible for performing are ERISA fiduciary activities.

ACTION ITEMS

Will my duties cause me to exercise discretion over plan assets or administration (hiring service providers, making investment choices, spending plan assets, etc.)? If so, I am a fiduciary and I need to make sure I understand and comply with my duties.

Does my plan document establish procedures for delegating fiduciary authority? If so, have I made a written delegation clearly identifying the scope of delegated authority?

RESOURCES AVAILABLE AT T. ROWE PRICE

FiduciarySource®—The T. Rowe Price PlanView Portal includes FiduciarySource®, your central source for fiduciary tools and information that can help you make informed fiduciary decisions.

T. Rowe Price would like to recognize Patrick T. Sheeran, Esquire, for his contributions to authoring this chapter.

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Patrick T. Sheerin has more than 28 years of legal and consulting experience in employee benefits, assisting clients with managing operational and fiduciary risks associated with their qualified defined contribution and defined benefit retirement plans and nonqualified executive deferred compensation plans. He consults with clients on plan design, implementation, and administration, and provides technical and strategic support on all aspects of Internal Revenue Code and ERISA compliance. Patrick also educates clients on emerging legal issues, and benefit trends, and advises them about compliance-related activities, including plan governance, document drafting, government filings, nondiscrimination testing, operational compliance reviews, and merger and acquisition due diligence and benefit integration.

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BASIC ERISA FIDUCIARY DUTIES 2

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Now that you understand what makes someone a fiduciary, it is important to understand the responsibilities ERISA places on plan fiduciaries. A fiduciary's performance of these legal duties will be measured in large part by the key concepts of "loyalty" and "prudence." In this chapter, we will also introduce you to the concept of "prohibited transactions" and some exceptions relevant to common plan activities.

Fundamental Fiduciary Duties: What You Need To Know And Do

LOYALTY

ERISA requires that fiduciaries act solely in the interest of plan participants and beneficiaries, for the exclusive purpose of providing benefits to them, and that participants pay only reasonable plan expenses. A fiduciary must administer the plan and invest the assets of the plan only for the benefit of the plan participants and not for their own benefit or the benefit of other fiduciaries, the company sponsoring the plan, or any other person. One court has colorfully described this "exclusive benefit" rule by saying that plan fiduciaries must make decisions with an "eye single" to the interests of the plan participants and beneficiaries.

As a plan sponsor fiduciary, however, you may receive "incidental" benefits from the plan such as providing a retirement plan as a part of a competitive compensation package for potential employees. A fiduciary may also pay reasonable expenses of administering the plan from the assets of the plan.

PRUDENCE

ERISA requires that a fiduciary act with the "care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person 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."

This "prudent person" rule is the cornerstone of a fiduciary's duty under ERISA and it has been described as being the "the highest known to the law." It is critical to understand that the test for evaluating a fiduciary's prudence in plan administration or investments is primarily one of process. The key issue in reviewing a fiduciary's action under ERISA is whether the fiduciary arrived at his or her decision by way of a diligent investigation of the issues at the time of the decision and whether there was a reasonable basis for the decision that was made.

If you are a fiduciary, it is important to note that your actions will be evaluated based on the "circumstances" that were "prevailing" at the time you made your decision. In simpler words, a fiduciary's actions are not judged with the benefit of hindsight. Not all decisions turn out to be right in the long run and not all investments are successful, but you as a plan fiduciary will not be liable if you used a prudent process in making your decision.

A prudent process includes obtaining sufficient information to understand the issues in the decision, and ensuring decisions have a reasonable basis. Keep in mind that, if a fiduciary doesn't have the knowledge or expertise needed to analyze a potential investment, or other plan decision, they need to seek out that information by engaging the services of a qualified consultant or adviser. If a fiduciary hires an expert, they will need to investigate the expert's qualifications, provide the expert with appropriate information, and satisfy themselves that their reliance on the expert's advice is reasonably justified.

Finally, remember the rule of "document, document, document." If a fiduciary's decisions are ever questioned, they need to be able to establish the steps they took in making them and the reasoning behind each decision. Be sure to document your fiduciary's actions in written records, such as meeting minutes. In addition, you should establish written procedures for operating your plan, and make sure that you follow them in practice.

> "Prudence" is the cornerstone of a fiduciary's duty under ERISA and the test for evaluating a fiduciary's prudence is whether the fiduciary arrived at his or her decision by way of a diligent investigatory process.

DIVERSIFICATION OF PLAN INVESTMENTS

ERISA plan fiduciaries are required to diversify the types of investments in the plan, to minimize the risk of large losses. Fiduciaries should consider the role a particular investment plays in the plan's overall investment portfolio, and take into account the risk of loss and the opportunity for gain associated with the investment. As part of a prudent process, as discussed above, fiduciaries must obtain sufficient information to understand the investment prior to making it. And the fiduciary's job does not stop there. Plan fiduciaries have an ongoing duty to determine whether plan investments are appropriate in the plan portfolio. As the U.S. Supreme Court has recently emphasized, in addition to prudently selecting investments at the outset, a plan fiduciary has a continuing duty to monitor plan investments and remove imprudent ones.

FOLLOW THE PLAN DOCUMENTS

Plan fiduciaries must "act in accordance with the documents and instruments governing the plan" to the extent they are consistent with the provisions of ERISA. You will need to be familiar with the provisions of your plan documents and follow them in practice. These documents include your plan's trust agreement and any investment policy statement that has been adopted for the plan. If the plan documents would somehow require you to act inconsistently with the law, then you cannot follow them.

Duties Specific to Roles

TRUSTEES

ERISA requires that all assets of an employee benefit plan be held in trust by one or more trustees, except for plans where the assets consist only of insurance contracts. Trustees of a plan under ERISA have, with certain exceptions, exclusive authority and discretion to manage and control the assets of the plan. One exception is that the plan document can provide that the trustees are subject to the directions of a named fiduciary who is not a trustee. This type of arrangement is quite common for plans and is referred to as a "directed trustee." In this instance, the trustee carries out the directions of the other fiduciary, if they are made in accordance with the terms of the plan and are not contrary to ERISA itself. One situation where this rule applies is when a plan provides that a committee of plan fiduciaries will have the power to direct the investments of the plan trust. In this case, the plan trustee, who has legal title to the assets of the plan, will acquire and dispose of assets of the plan in accordance with the proper directions of the committee. Directed trustees have significantly limited duties and responsibilities compared to trustees with discretion over plan assets.

Another important exception, which is very common with 401(k) plans, is where the plan permits participants to exercise control over the assets in their accounts. These plans are sometimes referred to as "participant directed" or "404(c)" plans. Such plans must provide for a broad range of investment options and plan participants must be provided with certain required information so they can make informed decisions. Once these requirements are met, plan fiduciaries will not be liable for investment losses caused by a participant's control over the assets of his or her account. The plan fiduciaries, however, must act prudently in selecting the investment options available under the plan.

INVESTMENT MANAGERS

The final exception to the plan trustee's exclusive duty to manage plan assets is where the authority to invest plan assets has been delegated to one or more investment managers. Investment managers under ERISA are limited to registered investment advisers, banks and insurance companies who have the power to manage, acquire, or dispose of plan assets and have acknowledged in writing that they are a fiduciary to the plan. ERISA provides that, if an investment manager has been properly appointed, then the trustees of the plan are not responsible for the decisions of the investment manager. However, a fiduciary who appoints an investment manager has to comply with the prudent person rule discussed above in selecting and appointing the investment manager. The appointing fiduciary also has a continuing responsibility to monitor the investment manager to make sure their performance is satisfactory.

> There are four fundamental fiduciary duties under ERISA: (1) duty of loyalty (i.e., acting solely in the interest of plan participants and their beneficiaries and with the exclusive purpose of providing benefits to them and paying only reasonable plan expenses); (2) duty of prudence (i.e., carrying out responsibilities prudently); (3) following the plan documents (unless inconsistent with ERISA); and (4) diversifying plan assets.

BEWARE OF PROHIBITED TRANSACTIONS

As discussed above, ERISA plans must be operated for the exclusive benefit of the plan participants. To avoid potential misuse of plan assets, the law prohibits many types of transactions between plans and other parties related to the plans. These parties include plan fiduciaries, relatives of plan fiduciaries and the company sponsoring the plan, who are defined as a "party in interest." Prohibited transactions include: direct or indirect sales or leasing of property between the plan and a party in interest, lending of money or other extension of credit between the plan and a party in interest, and the furnishing of services between the plan and a party in interest. The law does provide a number of exemptions allowing certain of these types of transactions to occur if the appropriate requirements are met.

Another category of prohibited transactions applies only to plan fiduciaries and is designed to prevent "self-dealing" by fiduciaries. These rules prevent a plan fiduciary from the following:

- dealing with plan assets in his or her own interest or for his or her own account,
- acting in any transaction involving the plan on behalf of a party whose interests are adverse to the interests of the plan or the interests of plan participants or beneficiaries,
- receiving any consideration for his or her own personal account from any party dealing with the plan in connection with plan assets.

As an example of self-dealing prohibitions, a fiduciary cannot receive "kickbacks" from someone who is providing services to the plan.

There are a number of "exemptions" for necessary transactions that would otherwise be prohibited, and the DOL has the authority to grant additional exemptions. One exemption allows the plan to hire a service provider (as long as the services are necessary to operate the plan and the compensation paid for those services is reasonable). Another important exemption permits plans to offer loans to participants (if offered on a reasonably equivalent basis, made in accordance with plan provisions, only a reasonable rate of interest is charged, and the loan is adequately secured).

OWNERSHIP OF PLAN ASSETS

Federal courts have exclusive jurisdiction over claims of fiduciary breach under ERISA. A consequence of this rule is that fiduciaries may not maintain the "indicia of ownership" of plan assets outside the jurisdiction of the United States District Courts.

CLAIMS FOR BENEFITS

ERISA requires that every plan provide an administrative procedure for handling claims of participants and beneficiaries for plan benefits. The claims procedure must be described in the summary plan description for the plan and must provide for written notice of any claim denial and the opportunity for a full and fair review of a denied claim. In other words, the plan must provide for an administrative appeal process after a benefit claim is initially denied. Regulations have been issued that provide specific procedures to be followed in processing benefit claims and the process must be completed within required timelines. Favorably for plan fiduciaries, benefit claimants are not allowed to file a lawsuit over their claim until they have completed the administrative claims process, and courts frequently provide deference to the decision reached in the administrative claims process.

> Prohibited transaction rules forbid potential self-dealing by plan fiduciaries—but there are exemptions for necessary and/or common transactions such as hiring a service provider and offering loans to participants.

ACTION ITEMS

If I am a fiduciary, do I keep records of meetings and decisions so that I can demonstrate my compliance with a prudent process?

Have I developed written procedures for routine fiduciary decisions? For example, do we have a process for making investment decisions or hiring service providers?

Have I asked plan counsel to make sure we are complying with any prohibited transaction exemptions that might be necessary?

RESOURCES AVAILABLE AT T. ROWE PRICE

Fiduciary Checklist—includes information one should consider to help ensure their plan is compliant; could help prepare for a potential audit.

T. Rowe Price would like to recognize R. Bradford Huss for his contributions to authoring this chapter.

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OVERSEEING INVESTMENTS 3

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One of the most important aspects of your retirement plan that requires care and attention is the plan's investment lineup. As a plan sponsor, it is critical for you to understand **who** has fiduciary responsibilities with respect to your plan's investments, **what** those responsibilities are, and **how** they may best be discharged. Of course, the answers to these questions can vary depending on the specifics of your plan, and getting professional advice tailored to your plan from a qualified expert may be useful. This chapter provides some basic guidance concerning the **who, what and how** of fiduciary oversight of plan investments.

Who is a fiduciary with respect to the plan's investments?

Whether a person is a fiduciary of a plan depends upon the *functions* performed for the plan, not the person's *title* or *position*. So while a plan's fiduciaries may ordinarily include discretionary trustees, investment advisers, and named fiduciaries such as investment or administrative committees, others may have a fiduciary role if they have decision-making power for the plan.

When it comes to the plan's investments, most defined contribution plans are set up so that the participants themselves can decide how to invest their plan accounts. Nonetheless, plan fiduciaries do have responsibility for choosing the investment options that will be made available to participants.

> Fiduciary roles with respect to plan investment options can vary—some plan sponsors may decide to appoint an investment committee responsible for selection and oversight, hire an investment adviser to provide professional advice, or outsource decision-making authority to an investment manager.

Fiduciary roles with respect to plan investment options can vary. Some plan sponsors decide to appoint an investment committee that is given decision-making authority with respect to the selection and oversight of plan investments. But not everyone who serves as a fiduciary is an expert in investments. For this reason, the plan fiduciary or fiduciary committee may decide to hire an investment adviser to provide professional advice. If the plan fiduciaries retain the decision-making authority, they can and should consider the professional advice, but they are still responsible for investment decisions for the plan. That said, plan fiduciaries may choose to outsource their decision-making authority to an "investment manager" fiduciary as contemplated by ERISA § 3(38). A 3(38) investment manager fiduciary assumes full responsibility for investment decisions for the plan, and must be someone with the requisite qualifications, such as a registered investment adviser (RIA). If you, as a fiduciary, decide to go this route, it is important that your delegation of authority to the 3(38) investment manager fiduciary be in writing and be clear as to what specific duties are being delegated. Even when you hire a 3(38) investment manager to select, monitor, and make changes to plan investments, you as the plan sponsor are still responsible for selecting that professional and for overseeing their performance.

What are the fiduciary's responsibilities with respect to plan investments?

The basic responsibilities of an investment fiduciary are selecting and monitoring the investment options that are made available under the plan, and the oversight of any plan investment managers.

Meeting these responsibilities requires a plan fiduciary to engage in an informed and thorough evaluation of the plan's needs and the options available in the marketplace. With respect to the plan's needs, every plan is different, and there is no one-size-fits-all approach. If you are responsible for the plan's investments, you may want to consider, for example, the characteristics of your employee-participants. For example, what is their average age? Do you have a large older population that is nearing retirement? What are their education levels? Are they sophisticated when it comes to finances and investments? With these kinds of considerations in mind, a fiduciary can look at the options available in the marketplace. But keep in mind that there are many available options, and there is no single, correct choice for any or all plans.

In evaluating the available options in light of your plan's needs, you may find it useful to understand some basic concepts about investments, including the *types* of investment vehicles available to retirement plans, *asset classes* and *management strategies* to choose from, and the *costs* associated with the available options.

> Regardless of the approach for overseeing investments, plan sponsors are still responsible for selecting investment professionals and overseeing their performance. This includes evaluation of a plan's needs and the options available in the marketplace.

TYPES OF INVESTMENTS VEHICLES AVAILABLE TO RETIREMENT PLANS

There are several different types of investment vehicles available to retirement plans, depending on the plan's needs and its size.

Mutual funds

Mutual funds are a popular choice for retirement plans. A mutual fund is a pooled investment vehicle managed by a professional asset manager that invests in an array of securities such as stock, bonds, money market instruments and similar assets, depending on the fund manager's strategy. Investors purchase shares of the fund, and the shares are valued on a daily basis, which means that investors are generally free to sell their shares. Mutual funds are registered with and overseen by the Securities and Exchange Commission (SEC), and are subject to certain disclosure requirements. As a result, publicly-available information about a mutual fund's investments, performance and fees is readily accessible, as are tools such as Morningstar.com that can help investors compare a mutual fund to other comparable funds.

Commingled pools

A commingled pool is a type of collective investment vehicle that combines assets from several sources to reduce the cost of managing each account separately, which may result in lower costs to investors compared to other investment vehicles. Examples of commingled pools include insurance company separate accounts or bank-sponsored common or collective trusts. The investment objective or style is set by the insurance company or bank, and access to these investments may be subject to higher investment minimums than mutual funds. Commingled pools are non-registered investment vehicles, which means that they are not subject to the same regulatory oversight as mutual funds, and information about their investments, performance and fees generally is not publicly available. While the commingled pool's manager will provide some disclosures to investors, the disclosures may not be as extensive as mutual funds are required to provide, and it may be more challenging to get information about other commingled pools to make comparisons.

> There are several different types of investment vehicles available to retirement plans in many different varieties, depending on the plan's needs and size.

Separate accounts

A separate account is an investment portfolio managed by a bank or an investment firm on behalf of a single plan sponsor. This structure may allow for more control on the part of the plan sponsor with regard to the separate account's investment strategy, but it also requires the sponsor to enter into a variety of service arrangements to obtain investment management, custodial, accounting, and other services for the separate account. Separate accounts tend to have high minimum investment requirements, but lower investment management fees than other investment vehicles. Separate accounts are non-registered investment vehicles, and information about their investments, performance and fees generally is not publicly available, and present some of the same benchmarking challenges as commingled pools.

Employer stock fund

An employer stock fund lets plan participants invest in the employer's company stock. These funds can be structured in different ways, but typically the fund is primarily invested in shares of the company. It may also hold some cash in order to ensure liquidity (the ability for investors to get out of the fund quickly, where permitted). Given the unique nature of these types of funds, there are special considerations that plan sponsors should keep in mind when their plan offers them. These considerations are discussed further below.

ASSET CLASSES, MANAGEMENT STYLES & ASSET ALLOCATION VEHICLES

The investment vehicles described above are available in many different varieties, depending on the types of assets that the vehicle invests in, and the management style and allocation strategies used by the fund manager.

Asset classes

An asset class is a category of investments that share particular characteristics. The main asset classes are: equities (stock), fixed-income (bonds), cash equivalents (money market instruments), real estate, and commodities. However, within each of these classes you will find a variety of options.

- Examples of stock funds include U.S. stock funds (e.g., Blue Chip Growth) or international and global stock funds (e.g., Asia Opportunities).
- Examples of bond funds include U.S. bond funds (e.g., Short-Term Bond) or international and global bond funds (e.g., Emerging Market Bond).

Management style

When investing in a particular asset class, a fund manager may utilize either "active" or "passive" management strategies. There are different costs associated with each type of strategy, which will result in different fees for investors.

- In an *actively-managed fund*, the manager actively analyzes and selects investments with the goal of outperforming the market. The fund manager will have a stated investment objective, and will utilize different analyses and trading strategies to attempt to achieve above-market returns. Actively-managed funds will likely have higher research and trading costs than passively-managed funds, resulting in greater overall expenses. The active fund manager's objective is to produce superior returns, even after fees are taken into account.
- In a *passive fund* the manager tries to achieve a return for investors that is comparable to the return of the overall market or a particular index, such as the Standard & Poor's 500 Index. A passively managed fund (or index fund) can usually operate at lower costs than an actively managed fund, resulting in lower overall fees to the investor.

Asset allocation vehicles (including target date funds)

Some investment managers combine the use of different asset classes and management styles to provide one-stop shopping for investors in the form of an *asset allocation vehicle*. An asset allocation vehicle invests in different asset classes over time in order to achieve a diversified investment portfolio geared toward either a target risk profile (such as conservative, moderate or aggressive—sometimes called a "lifestyle" fund) or a target retirement date (such as 2040 or 2060—sometimes called a "target date" or "lifecycle" fund). These vehicles can be structured as mutual funds, commingled pools, or separate accounts, and can utilize active or passive investment strategies (or a combination of both). Typically, these vehicles are structured to have an asset allocation strategy that changes over time, either to maintain a specific level of risk (in the case of lifestyle funds) or to decrease risk as the investor moves closer to retirement age (in the case of target date funds).

FEES ASSOCIATED WITH PLAN INVESTMENT PRODUCTS

The fees associated with plan investments are one component of a plan's overall expenses. Fees for investment management and other related services typically are assessed as a percentage of the assets invested in the fund (e.g., 0.50%). This is called the fund's *expense ratio*. The expense ratio may also be expressed in "basis points" (one basis point is equal to 1/100th of 1%). For example: 0.50% = 50 bps. These asset-based fees are deducted directly from investment returns and apply to all investors.

The *total expense ratio* for an investment option may reflect different component fees, including investment management fees, shareholder servicing fees or other fees. Fund expense ratios typically compensate the fund's management company for a variety of services, such as investment management, diversification, liquidity, communication, educational services, and administrative and recordkeeping services. However, when a fund is offered in a retirement plan, a portion of the fund's total expense ratio may be available to help offset the plan's administrative expenses. In this regard, revenue generated in connection with plan *investments* can be used toward plan *administration*:

For instance, when a fund is offered in a retirement plan, other service providers, such as the plan's recordkeeper, often provide services in connection with the plan's investment in that fund that would otherwise be performed by the fund or its service providers. For example, a fund's transfer agent usually has to keep track of shareholder positions in a fund. In 401(k) plans, the recordkeeper often fulfills that role. As a result of this arrangement, the fund avoids the expense of such services, which it would otherwise incur, and either the fund or its transfer agent may agree to pay a portion of its fees to the plan recordkeeper as compensation. These *administrative fee payments* by the fund or its service providers to the recordkeeper are sometimes referred to as "revenue sharing." Administrative fee payments are part of—and not additional to—the fund's total expense ratio, which highlights the importance of considering the plan's total fees when reviewing for reasonableness.

The amount of administrative fee payments available in connection with a plan's investments may depend on the *share class* of funds the plan uses. When selecting funds, plan fiduciaries should be aware that mutual funds may offer multiple share classes. Each share class represents a different investment option in the mutual fund. For example, a mutual fund may have a "retail" share class that is available to all investors, and an "institutional" share class that has a minimum investment requirement and is available to institutional investors such as large retirement plans. The total expense ratio for each share class may be different, and may result in different administrative fee or revenue sharing payments available to pay the plan's recordkeeper for administrative services. In this regard, the availability of different share classes may allow for flexibility in the plan's fee arrangement.

How does a fiduciary discharge its responsibility with respect to plan investments?

While plan fiduciaries are expected to act prudently in selecting investments for their plan, the good news is that investment decisions will not be judged based on hindsight. For example, choosing an investment that ultimately performs poorly due to unforeseen market conditions should not, in and of itself, result in legal liability. Fiduciaries are not judged by the results that they achieved for their plans, but rather on whether they acted prudently in making investment decisions. In other words, the *inputs* to the fiduciary's decision-making are more important than the *outcomes*. This puts a premium on the *process* that you, as a fiduciary, use to make investment decisions for your plan.

> Fiduciaries are not judged based on hindsight (i.e., they are not judged by the results that they achieved for their plans), but rather on whether they acted prudently in making investment decisions.

A good process will be thorough, consistently-applied and well-documented. Documentation of your decision-making process should make clear what information was considered and what decisions were made.

FOR EXAMPLE, A GOOD FIDUCIARY PROCESS IN OVERSEEING A PLAN'S INVESTMENTS MAY INCLUDE:

Understanding the plan document, which may set forth investment objectives or mandates for the plan.

- In addition to the plan document, investment fiduciaries should understand and consider any *investment policy statement* (IPS) that has been implemented for the plan. Although ERISA does not require it, some plan sponsors elect to establish an IPS that sets forth the plan's specific goals and objectives. The DOL has described an IPS as a written statement that provides the fiduciaries who are responsible for plan investments with guidelines or general instructions concerning various types or categories or investment management decisions. An IPS may describe the plan's investment structure and enumerate criteria and procedures for selecting, monitoring, and replacing investment options in the plan.
- There is no requirement that a plan sponsor utilize an IPS. However, should the sponsor choose to adopt an IPS, it is important that the IPS be carefully drafted. A "detailed roadmap" approach to drafting an IPS may provide comfort to decision-makers wanting clear direction on their selection and monitoring responsibilities. On the other hand, a less formal "framework" approach may help to avoid overly restrictive policy terms or policies that are too difficult to follow.
- The sponsor may benefit from input from the plan's consultant or any investment fiduciaries in drafting the IPS. If an IPS is adopted, it is important that the IPS is considered and followed by the plan's investment fiduciaries, and that the fiduciaries document their consideration of the IPS in making investment decisions for the plan.

Meeting regularly to discuss and review the plan's investments and keeping notes or minutes of such meetings.

Periodically reviewing the plan's investments, comparing the performance, expenses, and volatility of the plan's investment options to appropriate peer group and index benchmarks.

- For example, if a plan offers mutual fund options, plan fiduciaries can utilize publicly-available information to compare the funds' performance and fees to those of their respective categories as identified by Morningstar. The plan's service providers may also provide information that can assist with comparing the plan's investments to appropriate benchmarks, as may any investment consultant or adviser that the fiduciaries hire.
- When evaluating investment expenses, keep in mind that fiduciary prudence does not require the selection of the cheapest available option. What is important is that the fiduciaries consider available alternatives (including alternative share classes of funds) and the impact on the plan's overall expenses. For example, there may be instances where the selection of a fund share class with a higher total expense ratio is the right choice for your plan in light of the administrative fee payments that will be made to your plan's recordkeeper, which may avoid the need to assess other fees.

> A good decision-making process will be thorough, consistently applied and well-documented (i.e., documentation should make clear what information was considered and what decisions were made), and will utilize experts when needed.

Applying special considerations when it comes to default investment options, target date funds and employer stock funds.

- **Qualified default investment alternatives.** A plan may utilize default investment options for plan participants who are automatically enrolled in the plan and do not make affirmative elections as to how their plan accounts should be invested. Under DOL rules, a plan fiduciary will not be liable for any investment losses that occur as a result of automatically investing a participant's assets in a default investment option that is a qualified default investment alternative (QDIA). QDIAs are investment options that comply with DOL regulations that are designed to protect participants' interests even where they do not make affirmative elections with respect to their retirement savings accounts. Examples of investments options that the DOL has deemed appropriate for use as a QDIA include target date funds, balanced funds and managed accounts. Of course, QDIAs must be prudently selected and monitored just like other plan investment options.
- **Special considerations for target date funds.** Target date funds that share the same target retirement date may have very different investment strategies and risks. While these funds generally move to a more conservative allocation as the target retirement date approaches, some target date funds may not reach their most conservative investment mix until 20 or 30 years after the target date, while others reach their most conservative investment mix at the target date or soon thereafter. Plan fiduciaries should be aware of these and other differences when evaluating available options and consider these differences in relation to their priorities for addressing market risk, inflation risk, and longevity risk.
- **Special considerations for employer stock funds.** If a plan sponsor decides to make its company stock available as an investment option under the plan, proper monitoring of the employer stock fund will include ensuring that the investment fiduciaries and plan participants have information about the company's financial condition so that they can make informed investment decisions. In addition, participants must be given the opportunity to divest (sell) their investments in publicly-traded employer securities and reinvest their money in other diversified investments options in the plan. Where employee contributions to the plan are invested in company stock, the participants must have the right to divest immediately. Where employer contributions are invested in company stock, participants must be allowed to divest if they have three years of service. Some plan sponsors will limit the amount of employer stock a participant may hold in his or her account.

  Because of the potential for conflicts of interest where the company offers its own stock for investment by its employee benefit plans, some plan sponsors may elect to outsource the fiduciary oversight of their employer stock fund to an independent fiduciary in order to minimize risks. In that case, the independent fiduciary is responsible for evaluating the company stock, monitoring its performance, and making recommendations and decisions as to existing and new investments in company stock, or liquidations of plan holdings in company stock. In all events, it is important to remember that an employer stock fund should be monitored just like you would monitor other plan investments.

We know you take your responsibilities with respect to plan investments seriously, and we hope this information is helpful to you as a fiduciary. But keep in mind that being a plan fiduciary does not require you to be a financial expert. What is important is making thoughtful decisions as part of a consistent and documented process, and utilizing experts when needed.

ACTION ITEMS

Find out who is responsible for directing investments in your plan.

Consider setting up a formal investment committee if you don't have one.

Consider developing an investment policy statement documenting all of the plan requirements and processes.

Review company stock options (if any) for compliance, and consider engaging an independent fiduciary to help monitor the appropriateness of company stock as an investment option.

RESOURCES AVAILABLE AT T. ROWE PRICE

Plan and Investment Review—scheduled review of plan performance compared with a variety of benchmarks.

Investment Report Card—Summary of investment performance compared with relevant peer groups over multiyear periods.

T. Rowe Price would like to recognize Alison Douglass for her contributions to authoring this chapter.

ALISON DOUGLASS

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Alison Douglass is a partner in Goodwin Procter's ERISA Litigation Practice and has been recognized by Chambers USA as an "Up and Coming Practitioner" in her field. Alison has counseled and defended a broad range of clients, including 401(k) plan fiduciaries and service providers, in all phases of ERISA-related litigation, including pre-litigation counseling and a wide variety of trial and appellate matters in courts across the country. She has also represented clients in regulatory investigations and governmental proceedings, including before the U.S. Department of Labor and the Securities and Exchange Commission.

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OVERSEEING SERVICE PROVIDERS 4

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To properly administer your plan as a fiduciary it is likely you will need to retain professionals to advise and assist you. Selecting appropriate service providers is one of your most important responsibilities, and ERISA requires you to fulfill that responsibility 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."[1] This chapter discusses these duties, and will help you think through issues that commonly arise in the selection of service providers.

Selecting the Service Provider

As an ERISA fiduciary, you are required to reach "informed" decisions as you discharge your duties, meaning you must give "appropriate consideration to those facts and circumstances that... [you] know or should know are relevant..."[2] This requires you to employ what is commonly referred to as a "prudent process" in the selection of service providers—that is, a process that is informed and reasoned, and based on thorough investigation and deliberative evaluation. The appropriate process for selecting a service provider depends on the particular facts and circumstances, but always entails gathering relevant data and analyzing it thoroughly.

A prudent process for selecting service providers typically involves a number of steps, including assessing what kinds of service providers your particular plan would benefit from retaining, and identifying which specific service provider within each category you choose to retain is the best fit for your plan.

> A prudent process for selecting service providers typically involves assessing what kinds of providers your plan would benefit from retaining in light of the resources internally available to it, and identifying a provider within each category that is the best fit for your plan.

WHAT KIND OF SERVICE PROVIDERS DO YOU NEED?

There are a wide range of potential service providers you may need to employ to properly operate your plan. You should consider your plan's specific needs, in light of the resources internally available to it, to determine what kinds of service providers you should seek to hire. A few examples of commonly retained service providers are:

- Record-keepers
- Third Party Administrators
- Investment Advisors
- Investment Managers
- Plan Consultants and Advisors
- Fund Accountants
- Audit Services
- Plan Custodians
- Trustees
- Legal Counsel

[1] 29 U.S.C. §1104.
[2] DOL Advisory Opinions 29 CFR 2550.404a-1(b)(1).

HOW TO FIND SERVICE PROVIDERS WITH CAPABILITIES THAT MATCH YOUR PLAN'S NEEDS

For virtually all types of service providers, there are a variety of choices available on the market, offering different capabilities, approaches, and specific experience and expertise. If you were house-hunting, you would probably consider multiple options, rather than buying the first house you saw. And if you were hiring a babysitter for your children, you would probably consider the experience and background of each applicant. These same basic principles apply to selecting service providers for your plan.

So how do you find the right service provider? To find a good babysitter, you might ask other parents for recommendations. And to find the right house, you might use some combination of Internet research and advice from an experienced realtor. These approaches, appropriately translated to the plan administration context, are fine places to start. You might even consider hiring a plan consultant or advisor who specializes in identifying service providers that are good fits for plans. Whatever specific process you choose to employ, you will likely find it useful to identify multiple options, obtain relevant information about them, and thoroughly kick the tires on each before making a final decision.

One powerful tool you can use to generate a list of qualified service providers, and gather key information about them, is soliciting bids, typically through a Request for Proposal (RFP). You can use an RFP to provide potential bidders with relevant facts about your plan, establish a timeline for the bidding process, and elicit information from prospective providers that can help you make an informed and reasoned decision. There is no minimum number of service providers whose bids must be solicited or considered, but it is useful to have a sufficient number to allow for a meaningful comparison.

Plan fiduciaries may find the following types of information helpful when selecting a service provider:

- **Nature of the firm.** Information about the firm's size, financial condition, and experience with retirement plans of similar size and complexity.
- **Quality of the firm's services.** Information about the firm's experience and track record; the identity, experience, and qualifications of the specific professionals who would handle your plan's account; and any recent litigation or enforcement actions taken against the firm.
- **Description of business practices.** Information about the firm's approach to providing the services in question. For example, if you are hiring an investment consultant, you might ask how the firm identifies, evaluates, and monitors investment options. You might also inquire whether the firm has fiduciary liability insurance.
- **Required licenses and bonds.** If the service provider will handle plan assets, make sure the provider has an appropriate fidelity bond, which protects the plan against loss resulting from fraudulent or dishonest acts. You may also want to verify that the service provider has any required licenses (i.e., verifying that an attorney is in good standing with the bar), and check to see if there are any pending complaints against the provider.
- **Oversight & Commitment to a Fiduciary Standard of Care.** If the service provider is being retained to act in a fiduciary capacity, consider confirming that the provider accepts its fiduciary responsibilities in a suitable manner, and has fiduciary compliance and training structures in place to ensure compliance with relevant laws and regulations.
- **Conflicts of Interest.** It is a best practice to gather information necessary to understand whether a provider's relationships to other firms could present conflicts that might impair the provider's ability to render services solely in the best interests of the plan. There are numerous recognized mechanisms that can be used to resolve or mitigate potential conflicts. As the hiring fiduciary, your job is simply to identify potential conflicts and prudently consider whether measures are in place that will adequately protect the plan's interests.

The information you gather, considered in light of the specific characteristics of your plan (such as its size, goals, and participant profile), will help you identify service providers whose service level, approach, and fees best match your plan's specific needs.

FEES AND COMPENSATION

Where the plan (rather than the plan sponsor) is responsible for paying a service provider's fees, the service provider's compensation becomes an important consideration that should be carefully evaluated. Fees diminish the assets of the plan, and can have a significant impact on plan participants' retirement savings. Consequently, few issues have produced more litigation against plan fiduciaries than alleged failure to properly consider service provider compensation arrangements.

ERISA requires that the fees paid to a service provider be "reasonable." The reasonableness of fees must be assessed in light of the services to be performed, the provider's qualifications, the scope of the services being provided, and market rates—that is, the fees charged by competitors for comparable services. Popular methods used to determine the "reasonableness" of fees include competitive bidding processes, expert opinions, and benchmarking services.

> ERISA requires that fees paid to a service provider be "reasonable"—few issues have produced more litigation against plan fiduciaries than alleged failure to properly consider service provider compensation arrangements.

A general benchmarking study can provide a good starting place to assess the reasonableness of fees. Such studies collect industry data to approximate the appropriate range of fees for particular services. This basic type of benchmarking study can help ascertain general market rates, but generally does not take into account the specific objectives and service requirements of particular plans. Competitive bidding processes and (where appropriate) expert opinions can provide more tailored information.

Another important tool that can be used to assess the compensation received by certain service providers is the provider's 408(b)(2) disclosure. Department of Labor regulations implementing Section 408(b)(2) of ERISA require certain plan service providers, including providers of brokerage and recordkeeping services, to disclose information about the various forms of compensation they receive, both direct and indirect.

Indirect compensation earned by service providers can take many forms, such as "float income" that some service providers earn on retirement contributions that are pending investment, or "revenue sharing" or "administrative fee" payments that some investment options in which plan assets are invested make to certain service providers. Although your plan does not pay such compensation directly to the service provider, it is nevertheless compensation the service provider earns as a result of its retention by your plan. This makes it something of value your plan offers to the service provider that should be taken into consideration when negotiating fees.

Generally speaking, you will not want to select a service provider based on any one factor. You may want to take into account several of the factors discussed above, as well as additional considerations that may be specific to your plan.

Special Considerations Pertaining to Retaining Help in Selecting Your Plan's Investment Line-up

Many plans engage an investment advisor to provide guidance regarding the selection and monitoring of plan investment options. There are different kinds of service providers available to plans that provide help selecting investment line-ups, and your fiduciary responsibilities will depend on the nature of the arrangement you select.

One option is to engage an investment advisor to act in a consulting capacity. With a consulting arrangement, the advisor will provide investment advice to you to aid your decision-making, but you will retain ultimate responsibility for deciding what investment options should be selected. Investment advisors hired pursuant to ERISA 3(21) owe fiduciary duties of prudence and loyalty when they provide investment advice. Other sources of investment advice may not be subject to fiduciary duties. Whatever the source of investment advice you receive, so long as you retain final decision-making responsibility over the plan's fund line-up, ERISA does not permit you to mechanically adopt the advice you receive. Rather, you are required to employ a prudent process, "channeling your inner skeptic" to appropriately probe the offered advice so that if you do ultimately accept it, you can demonstrate that your reliance was reasonable.

A different option is to engage an investment manager under ERISA 3(38), who will assume full responsibility for the plan's investment decisions. A 3(38) investment manager is delegated full fiduciary responsibility for selecting fund managers, monitoring them, and making any necessary changes. If you hire such an investment manager, your fiduciary responsibility will be limited to monitoring the manager to ensure it is appropriately fulfilling its responsibilities. As might be expected, the increased responsibilities and increased fiduciary risks assumed by 3(38) investment managers typically command a higher price than investment consultants, and you should carefully consider which kind of arrangement is most suitable for your plan.

Service Provider Contracts

It is a good idea to maintain updated written agreements with all service providers. This will help you monitor the service providers, and will also make it easier to respond in the event of an audit by the Department of Labor, which may include a review of all service provider contracts.

Your contracts with service providers must have reasonable termination provisions, so that the plan is not unreasonably locked into a long-term arrangement that becomes disadvantageous.[3] You should take particular care to assess any provisions that impose termination penalties for their potential impact on the plan.

[3] 29 C.F.R. § 2550.408b-2(c).

Monitoring the Service Provider

After a service provider is selected, you are under a continuing duty to monitor their performance. This includes reviewing and analyzing the performance of service providers at reasonable intervals. The review should, among other things, ensure that the service provider is complying with the terms of the plan and all applicable statutory standards. There is no specific requirement regarding the frequency of the review, but you should regularly assess the appropriateness of both the fees and services offered.

Actions you may take to ensure that service providers are appropriately providing all agreed-upon services include:

- Evaluating any notices received from the service provider related to possible changes in compensation or other information that was provided to the plan at the time of hiring;
- Reviewing any reports provided;
- Checking actual fees charged;
- Asking about policies and practices; and
- Following up on participant complaints.

Your review should include a periodic assessment of the reasonableness of the service provider's compensation, and should consider all aspects of the provider's compensation package, including expense reimbursements, indirect compensation the service provider receives from third parties, and limitation of liability provisions.

> After a service provider is selected, you are under a continuing duty to monitor the service provider's performance and periodically assess the appropriateness of both the fees and services offered.

One method that can be used to monitor the reasonableness of fees is to issue periodic RFP's or Requests for Information ("RFI"). The RFI is a limited form of RFP designed to elicit information regarding fees and expenses. This information can then be used to assess whether the current service provider's fees and compensation remain reasonable.

It is a best practice to document your process both for selecting and monitoring service providers. This provides you an opportunity to preserve a description of the processes you employed, as well as the reasoning behind your choices. Such a record may prove useful in the future if questions arise concerning your selection or monitoring.

ACTION ITEMS

Am I familiar with the requirements of 408(b)(2)?

Conduct a periodic review of service providers to ensure that service and performance standards are being met.

Document the review/meetings and issues discussed as well as any decisions made during or as a result of the review/meetings.

Review the fees (direct and indirect) of service providers to assess the reasonableness of fees and whether any conflicts exist.

Conduct an in-depth review of service providers periodically to ensure that your fees and arrangements are consistent with current practices and costs and to determine whether a new RFP process is warranted.

RESOURCES AVAILABLE AT T. ROWE PRICE

Plan Cost Analysis—allows you to view and compare fees paid by your participants.

408(b)(2) Disclosures—T. Rowe Price provides a summary disclosure document, which outlines general recordkeeping services as well as fees, investments, and compensation specific to your plan.

Fiduciary Benchmarking—can help plan sponsors meet their fiduciary obligation to determine if plan fees are reasonable as defined in ERISA section 408(b)(2).

T. Rowe Price would like to recognize Gregory F. Jacob for his contributions to authoring this chapter.

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HELPING PARTICIPANTS 5

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What Does “Helping Participants” Mean?

You already know fiduciaries are required to act solely in the interest of the plan participants (after all, a significant portion of this guide is devoted to describing your legal obligations as a fiduciary and how to carry them out). Given that, you might be asking yourself why this chapter is entitled “Helping Participants” and how this is different from the fiduciary duties and obligations we’ve already discussed.

What’s different is that this chapter focuses on how your plan interacts with your participants. While some of this interaction involves fiduciary obligations and mandatory compliance issues—such as required disclosures and communications with participants—helping your participants goes beyond compliance issues. This includes considering optional plan features, like automatic enrollment, education, or investment advice. Your plan may be in full compliance with the rules, but your participants may not be making the most of the retirement savings opportunity you provide.

Helping Participants—The Required Compliance Issues

As you know from reading other chapters in the guide, as well as from your own experience if you are a plan fiduciary, the law is full of requirements for properly structuring and administering your company’s retirement plan. That is also true with respect to helping participants.

In addition to statutory requirements built into the law by Congress, the Department of Labor (“DOL”), which is generally responsible for the reporting and disclosure requirements of ERISA, has promulgated several regulations specifying when and how your plan is to help participants understand their rights and obligations under the plan. These include periodic benefit statements, distribution of the Summary Plan Description and the Summary of Material Modifications, Black-Out Notices, and 404a-5 participant disclosure notices. We will discuss each of these below.

Helping Participants—Beyond Basic Compliance

While the law requires certain duties and imposes a basic structure on your retirement plan, it also gives your company latitude to design a plan that fits your specific needs. For example, your company may choose to offer a matching contribution or not. Your company can develop specific eligibility criteria fitting your workforce. As a fiduciary, you can also choose whether to provide participant education or investment advice. This flexibility is intended to make it possible for more employers to offer a plan. In practice, it also means that your plan may be able to adopt features that improve certain outcomes for participants, even though those features are not required.

For example, do you know what proportion of your eligible employees participate in the plan? What the average participant’s deferral rate is? How long it has been since the average participant changed his or her investment allocation? These are questions that might help you evaluate how well your plan is working for your participants.

Remember, so-called plan “optimization” (adopting plan features and services intended to improve outcomes like participation or deferral rates) is not by itself part of your fiduciary duty—neither your company as a plan sponsor, nor you as a fiduciary, have an obligation to adopt automatic enrollment, for example. However, if you do adopt them, you are responsible for properly implementing them and operating the plan going forward. We will discuss these issues in more detail below.

Mandatory Participant Interactions

In general, the required participant communications and disclosures are intended to ensure that participants have been informed of their rights and obligations under the plan. Some are periodically required, while others are triggered by certain events. There can be civil penalties imposed for a failure to provide some notices, while other violations are a fiduciary breach. Which notices are required, and the timing of such notices is often dependent on the type of plan. For example, a participant-directed, defined contribution plan (like most 401(k) plans) requires sending quarterly benefit statements to participants, while a traditional defined benefit plan must send a benefit statement only once every three years.

In general, it is the responsibility of the Plan Administrator (often the named fiduciary of the plan) to ensure the plan is complying with these requirements, but this fiduciary authority may be delegated to other fiduciaries. Please remember that a recordkeeper or Third Party Administrator (TPA) is typically not a plan fiduciary, and is not the Plan Administrator in most cases.[1] It is quite likely, however, that the plan fiduciary has hired a service provider to assist in making and distributing required notices. A good compliance plan and close coordination with service providers will help ensure that the right notices go out at the right times and help avoid penalties that might be attached to certain notices.

Here are some of the most common required participant assistance documents and notices:[2]

PARTICIPANT-DIRECTED, INDIVIDUAL ACCOUNT PLAN PARTICIPANT DISCLOSURES (APPLICABLE TO MOST 401(k) PLANS)

Most 401(k) plans are participant directed, individual account plans—this means the participants decide how to invest their accounts among the options on the plan investment menu. The DOL participant disclosure regulation (often referred to as a 404a-5 disclosure) requires the Plan Administrator to disclose to participants certain plan and investment-related information, including fee and expense information. Some of the information is provided via the plan documents, while other required information is provided through the quarterly benefit statement, in a separate annual notice, and on a required website.

The concept behind the rule is fairly simple: because the plan gives participants the responsibility to make investment decisions, it has a duty to provide specified basic information about the plan and its investments to help participants to make informed decisions. Though the regulation has a number of specific requirements, the core of the participant disclosure regulation is a comparative chart that lists in one place all the basic investment information participants need to know. The intention is to give participants an easy way to review the minimum information needed to evaluate plan investment options—additional information beyond the minimum requirement is available upon request, including a website with more current and detailed information than is provided in the chart.

The comparative chart allows the participant to make "apple to apple" comparisons of investment products available in the plan. The chart must list the plan's investment options and briefly describe what kind of investment each option is. It must also provide (where applicable) a 1-, 5-, and 10-year performance history of the investment option, a benchmark to compare this performance with, and aggregated fee information regarding investment costs.

> Required participant communications and disclosures are the responsibility of the plan administrator (typically, the named fiduciary of the plan) and are intended to ensure that participants have been informed of their rights and obligations under the plan.

[1] Typically, the 3(16) plan administrator is the person signing the Form 5500 for the plan—even if the Form is prepared by someone else, the 3(16) plan administrator is required to sign it in his or her fiduciary capacity.

[2] There are a variety of less common notices and disclosure requirements not addressed here. A good overview is provided in the Department of Labor publication "Reporting and Disclosure Guide for Employee Benefit Plans."

402(F) ROLLOVER DISTRIBUTION OPTIONS NOTICE

The Tax Code requires that a 402(f) notice be sent to a participant in a 401(k) or other qualified plan 30 to 180 days before the participant receives a plan distribution that is eligible as a rollover distribution. An eligible rollover distribution is a distribution from a plan that can either be rolled over to another plan or to an Individual Retirement Account ("IRA").

The purpose is to ensure that participants understand their distribution options and the tax and other potentially serious consequences of the option they select. The 402(f) notice is a comprehensive, plain-language explanation of a participant's distribution options and how distributions will be taxed, including possible special tax treatment (such as a 10% early distribution penalty). The IRS provides model notices for use. In practice, a plan service provider, such as the plan record-keeper, typically prepares and distributes the notice.

PERIODIC PENSION BENEFIT STATEMENTS

Participant-directed, individual account plans must provide quarterly benefit statements. In addition to showing the account balance and investment performance, the quarterly statement must show the dollar amount of any fees removed directly from the account during the quarter. Alternatively, if fees are charged internally to the investments and reflected in the investment returns, the statement must provide a notice explaining this. The statement must also explain the importance of diversification. A defined contribution plan with no participant direction must provide an annual statement, and a defined benefit plan must provide a notice every three years.

SUMMARY PLAN DESCRIPTION (SPD)

This document is given to employees within 90 days after they become a participant in the plan. The SPD provides a basic description of the plan, including notice of a participant's rights and responsibilities, and offers an overview of plan features and benefits. SPDs must be provided every 5 years, even if there has been no change to the plan. Because the SPD is the primary document explaining the plan terms to participants, it is important that the SPD be kept updated directly or through SMMs (see below) and that it accurately reflect the terms described in the plan document.

> Discrepancies between the plan document and the SPD have been the basis for costly litigation for plan sponsors.

SUMMARY OF MATERIAL MODIFICATION (SMM)

The SMM lets participants and beneficiaries know of changes to the plan or to the information in the SPD. The SMM must be provided to participants within 210 days after the end of the plan year in which the change was adopted. As with the SPD, it is important that the SMM accurately and timely reflect changes to the plan terms.

SUMMARY ANNUAL REPORT (SAR)

The SAR provides plan participants with the financial information contained in the plan's annual Form 5500 report and is distributed annually to participants (typically two and a half months after the plan files the Form 5500).

BLACKOUT PERIOD NOTICE

If the plan schedules a "blackout" period during which it does not allow participant and beneficiary transactions for at least three consecutive business days (such as might occur when a plan changes recordkeepers), the plan must provide advance notice of at least 30 but not more than 60 days to participants.

NOTICE FOR "MAPPING" INVESTMENTS

This notice alerts participants of an investment change due to an investment option closing or a change in service providers. It will clearly illustrate how existing balances and future contributions will automatically move (or map) over to an investment with similar objectives. Participants will be given the opportunity to make investment changes prior to the mapping date as well as after the mapping has occurred.

PROSPECTUS FOR EMPLOYER SECURITIES IN THE PLAN

Publicly-traded corporations that offer an employer stock fund as an investment option in their 401(k) plan have an obligation to furnish participants with not only the SPD, but also a prospectus required by the Securities Act of 1933. For convenience and consistency, it is not uncommon for plan sponsors to combine the SPD and prospectus into a single document. Recent court decisions have suggested that keeping these documents separate, rather than combining them, may prevent a plan fiduciary from being responsible for any errors the prospectus may contain.

EVOLVING REQUIREMENTS

Fiduciaries should remember that the notice and disclosure requirements are not static. The Labor Department and other regulators are considering regulations that may require additional notices. For example, the DOL is considering requiring quarterly benefit statements to include retirement income projections. A regulation was proposed, but has not yet been finalized. Similarly, DOL proposed but has not yet finalized a regulation specifically addressing disclosure requirements unique to Target Date Funds.

Elective Plan Features Affecting Participants

As we discussed above, plan sponsors may elect a variety of customized features for their plans. While there are many reasons to consider these features, some of them have been demonstrated to increase participation and savings rates, helping participants better utilize the retirement savings opportunities provided by their employers.

While plan fiduciaries typically are not required to consider improvement in these outcomes as part of their formal fiduciary obligation, they do have an obligation to properly administer the plan once such choices have been made. For example, there is no fiduciary obligation to adopt automatic enrollment, but having done so, the plan fiduciary must properly administer the plan.

> Adopting plan features and services intended to improve outcomes is not by itself part of your fiduciary duty—however, if you do adopt them, you are responsible for properly implementing them and operating the plan going forward.

404(c) PLAN STATUS AND PARTICIPANT DISCLOSURES

A basic issue for a participant-directed plan is whether it wants to elect status as a 404(c) plan. Fiduciaries to plans that require participants to make their own investment decisions, such as most 401(k) plans, are responsible for prudently selecting and monitoring the menu of available investments. However, unless the plan has formally and properly elected 404(c) status, those fiduciaries may also be responsible for the decisions of each individual participant on how to invest his or her account among the options on the plan menu.

If a plan complies with regulations issued by the DOL implementing §404(c) of ERISA, then the participants, not the plan fiduciaries, are responsible for the results of their investment choices. While the plan fiduciary in a 404(c) plan is not liable for investment losses flowing from the participants' investment decisions, the plan fiduciary is still responsible for selecting and monitoring the investment options available in the plan, as well as for seeing that participant investment instructions are carried out.

The 404(c) regulation was adopted roughly 20 years ago, so some of its conditions regarding investment options and trading frequency may seem surprisingly easy to meet. However, the disclosure requirements of the regulation are more challenging, and require careful attention. To qualify for 404(c) status, the regulation requires the plan to:

- offer at least three investment options with materially different risk and reward characteristics, allowing participants to diversify their investments and select their desired risk profile;
- give participants the ability to exercise independent control over assets in their accounts and to make investment changes at least quarterly;
- provide participants with adequate investment information with which to make investment decisions—specifically, a fair and balanced presentation of the investment options that is easily accessible to all employees, accurate, and timely (the 404(a)(5) participant disclosure has provided more clarity to this requirement); and
- Identify itself as a 404(c) plan to plan participants and to select 404(c) status on the Form 5500.

AUTOMATIC ENROLLMENT AND QUALIFIED DEFAULT INVESTMENT ALTERNATIVES (“QDIAS”)

Deciding to adopt automatic enrollment can have a significantly positive effect on the retirement readiness of plan participants. It can also help the plan pass required nondiscrimination testing intended to prevent the plan from benefiting only higher-income employees.

Automatic enrollment materially increases participation in the plan, benefiting those workers who would otherwise not participate. According to the Department of Labor, only ⅔ of eligible workers in a typical plan affirmatively choose to become plan participants. Where a plan adopts automatic enrollment, participation rates can increase to more than 90%.

If the plan decides to use qualified default investment alternatives (QDIAs) as the default investment for automatically enrolled participants, and if it meets the notice and other requirements of the regulation, the fiduciary receives limited fiduciary relief from the investment outcomes of automatically enrolled participants.

How Automatic Enrollment Works

Automatic enrollment is a plan design feature than can offer many benefits but needs to be considered in light of the particular facts and circumstances of each plan. Though there are different types of plan designs using automatic enrollment, the common feature is that workers must “opt out” rather than “opt in.” Workers are given notices informing them that, unless they decide not to participate in the plan or unless they provide different instructions for handling their money, they will be enrolled in the plan. Specified contributions will be deducted from their paychecks and invested in plan options that typically are QDIAs.

If the workers do not provide alternative instructions, they are considered to have agreed to the arrangements described in the notices as if they had affirmatively selected them. The plan fiduciaries are responsible for the selection and monitoring of the investment options, but not for the investment results of the automatically enrolled participants (if a QDIA is used and the requirements of the QDIA regulations are satisfied).

What Are QDIAs?

QDIAs are certain investment options (examples include life-cycle or target date funds, balanced funds, and managed accounts) that comply with DOL regulations designed to protect the interests of workers in situations where the workers do not directly provide investment instructions. In addition to automatic enrollment, QDIAs can be used for investing profit sharing and money purchase plan contributions, for plan conversions (moving the plan from an old investment menu to a new one, such as when a plan changes service providers), or for rollover contributions.

Automatic Enrollment Notice Requirements

As part of the automatic enrollment notice, investment information about the QDIA must be provided. The notice must give eligible employees advance notice that they will be automatically enrolled in the plan, including the percentage of their withheld contributions and the QDIA into which their contributions will be invested. Employees are also given the opportunity to select their own investments or to opt out of the automatic enrollment feature.

The exact timing of the notice depends on the structure of the plan.

PARTICIPANT EDUCATION AND INVESTMENT ADVICE

In addition to required information about the plan investments, many plan sponsors offer participant education programs to help participants make informed investment decisions. A growing number of sponsors also offer investment advice services, in which participants receive specific investment recommendations from investment advisors.

> In addition to required information about the plan and its investment options, many plan sponsors offer participant education programs to help participants make informed investment decisions.

Knowing where ERISA draws the line between education and advice is important because not all advisors can provide fiduciary advice to participants under the prohibited transaction rules. DOL Interpretive Bulletin 96-1 ("IB 96-1") explains the difference.[3] Fiduciary advice is an individualized recommendation to the participant regarding investments available under the plan. Education is more general information, such as facts about the plan and its investment options, or information about general investment strategies, such as the importance of diversification or the meaning of "dollar cost averaging." Education may also include individualized model asset allocation portfolios by asset class.

Many service providers cannot provide fiduciary participant advice because they have a financial interest in one or more of the plan's investment options that would give rise to a prohibited transaction.

Targeted Communications and Education

Communications can enhance employee participation in your defined contribution plan and help participants make the most of this important benefit. Many plan sponsors exceed the minimum participant communication requirements with standard broad messaging. However, sponsors may get more participant engagement by using targeted communications that can improve participant outcomes while helping sponsors achieve plan-wide goals.

These optional communications can be delivered in print, electronically, or in plan meetings, and can cover a range of topics, such as:

- the importance of plan participation
- goals for retirement savings
- the importance of diversification
- the effect of compounding returns
- the tax benefits of plan participation
- model asset allocations by age or risk tolerance

Helping Participants: In Conclusion

In addition to the required participant communications and disclosures intended to help participants make informed decisions about savings and investment, plans may elect optional features that can significantly increase the retirement readiness of their workforces. Features such as automatic enrollment, and the availability of investment education or advice, can improve outcomes, having an impact outside of the plan. For example, employees who are prepared for retirement may be more likely to retire, while workers who are not prepared may intend to remain with the company longer than anticipated. Retirement plans are an important part of the human resources plan for the company as a whole.

[3] The DOL rescinded IB 96-1 as part of a new definition of education in a regulation that was in effect only from June 2017 through June 2018. Following litigation challenging the validity of the new regulation, the regulation was vacated *in toto* in 2018 by the U.S. Fifth Circuit Court of Appeals. While DOL has been silent regarding the renewed applicability of IB 96-1, the court's action means that no provision in the vacated rule—including the new definition of advice—has any effect. As a result, it is likely that IB 96-1 again applies as of June 2018 despite DOL's lack of an affirmative statement.

ACTION ITEMS

Have I talked to my service providers about helping me provide required participant disclosures?

Provide ongoing and accurate communications on investments and plan features (e.g., loans distributions, contributions, etc.).

Distribute information to all eligible employees regarding the investment options available under the plan.

Consider conducting educational meetings and providing general financial/investment information.

Does my plan use automatic enrollment and/or QDIAs? While not required, automatic enrollment can substantially increase the participation rates for employees and may help the plan pass or provide a safe harbor from nondiscrimination testing.

RESOURCES AVAILABLE AT T. ROWE PRICE

Investment Advice—T. Rowe Price can offer plan sponsors access to third-party advisory services (i.e., Morningstar and Financial Engines advisory services) that can help plan participants choose investments.

Targeted Messaging—T. Rowe Price can help deliver an effective communication strategy that takes into account the fact that participant behavior and priorities change over time.

Meetings That Motivate—T. Rowe Price can provide on-site and Web-based employee meetings to help them understand their options.

Robust Web Communications—The T. Rowe Price Workplace Retirement Site includes guidance, planning tools, and education.

Participant Fee Disclosures—T. Rowe Price can help you fulfill your fiduciary responsibility to provide participant fee and investment disclosures.

T. Rowe Price would like to recognize the Hon. Bradford P. Campbell for his contributions to authoring this chapter.

THE HON. BRADFORD P. CAMPBELL

Partner, Drinker Biddle & Reath LLP

Bradford P. Campbell is a nationally recognized figure in employer sponsored retirement, health, and other welfare benefit plans. From 2006 to 2009, he served in the federal government as the Assistant Secretary of Labor for Employee Benefits, and the head of the Employee Benefits Security Administration (EBSA). As ERISA's former "top cop" and primary federal regulator, Mr. Campbell provides clients of Drinker Biddle & Reath LLP with insight and knowledge across a broad range of ERISA plan-related issues.

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PLAN ADMINISTRATOR BASICS 6

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In this chapter, we'll discuss qualification requirements under the Internal Revenue Code, IRS audits, and correcting plan document and operational errors. Although they are not fiduciary functions, these are important rules with significant consequences for noncompliance.

Section 401(k) plans must meet special rules, many of which come from the federal tax code. Other retirement plans must also meet special rules if they are to enjoy favorable tax treatment. This tax treatment not only helps the plan, it also helps plan participants and the sponsoring employer (or other plan sponsor). (For most plans the employer will be the sponsor, so we'll just refer to employers, rather than plan sponsors, in the rest of this chapter.)

THE TYPES OF RETIREMENT PLANS SUBJECT TO SPECIAL TAX CODE RULES INCLUDE:

- 401(k) plans
- profit sharing plans
- employee stock ownership plans (ESOPs)
- money purchase pension plans
- stock bonus plans
- defined benefits plans

In addition to fiduciary duties specified under ERISA, qualified retirement plans (and other retirement plans) are subject to Internal Revenue Code (i.e., federal tax law) requirements relating to, for example, plan document and nondiscrimination requirements.

You Need a Plan Document

It is important that you follow the tax code rules that apply to your retirement plan. Those rules require that you have a written plan document. Your plan document should be formally adopted by your company, and it should be kept up to date. Your plan document will probably be lengthy. That is because it must state many of the tax code rules that apply to your plan.

The tax code's rules can affect many important aspects of your retirement plan, including:

- who may (or must) be covered under your plan
- how much employees may contribute to your plan
- how much your company may contribute in matching or other contributions
- when participants will become vested in your plan benefits
- when and how plan benefits will be paid to participants

Section 401(k) plans and other retirement plans that meet these special tax code rules are sometimes called "qualified" plans. Other types of retirement plans must also meet special rules set forth in the tax code, but they are not called "qualified" plans.

These include:

- Section 403(b) plans (also known as "tax-sheltered annuities")
- Section 457 plans

The tax code rules that apply to Section 403(b) and Section 457 plans are different from those that apply to qualified plans, but they are just as important.

IRS Review of Plan Document

The tax code rules that apply to your retirement plan are complicated, as are the rules that must be included in your plan document. To help employers ensure that their plan documents include the required provisions, the IRS is willing to review those documents both when a plan is first adopted and when it is being terminated.

FAVORABLE DETERMINATION LETTER

This IRS review helps you determine if your plan document includes the required provisions. If it does, the IRS will issue a favorable "determination letter." Your company is not required to request this IRS review, but it may be helpful. To request a review, you must file a determination letter application with the IRS.

The IRS charges a "user fee" for looking at your plan document and making its determination.

WHEN CAN YOU REQUEST A DETERMINATION LETTER?

The IRS will review an employer's plan when it is adopted and when it is terminated. The IRS has said that there might be some circumstances where it will look at a plan document after it is first adopted and before it is terminated, but it has not yet described those circumstances.

PREAPPROVED PLANS

An alternative to filing a determination application is for your company to adopt what is called a "preapproved" plan document. For these preapproved plans, a financial services company, law firm, or other organization will have asked the IRS to approve a form of a plan document (the preapproved plan). This preapproved document will allow you to make certain choices about the design of your plan from a preestablished list of options.

You will normally have choices as to:

- which employees will be eligible and when
- what types and amounts of contributions will be made
- how quickly employees will be vested in their benefits
- when and how employees will be paid their benefits

You make these choices using an adoption agreement that your company signs. This adoption agreement is coupled with a longer, basic plan document that describes your plan's provisions in greater detail.

In the case of a preapproved plan, the organization sponsoring your plan will receive an "opinion" letter from the IRS. Although this is not technically the same as a "determination letter," it is an indication that the IRS has examined, and found satisfactory, the language of the preapproved plan document.

Assuming that you choose only from among the options offered in the adoption agreement (and do not make other changes to the plan document), this should give you some measure of comfort that the IRS is satisfied that your plan document includes the required provisions.

KEEP YOUR PLAN UP TO DATE

It is important to follow the terms of your plan document. It is also important to make sure that the your "summary plan description," or SPD, is distributed to participants and accurately summarizes your plan. As changes are made to your plan, participants must be provided with an updated SPD or receive a separate summary of those changes, called a "summary of material modifications" or "SMM." Even if SMMs are distributed in a timely fashion, participants should receive a complete, updated SPD every five years.

TIMING OF PLAN AMENDMENTS

You may take some comfort in having a favorable determination letter for your plan or a preapproved plan with an opinion letter from the IRS. However, there is no guarantee that the IRS will not later challenge either the plan language or the way your plan has been operated. It is especially important that any amendments to your plan document be adopted in a timely way. Sometimes, you will have to amend your plan because of a change in the tax code. If you do, Congress may specify the deadline for adopting that amendment.

If Congress does not specify a deadline, the IRS will typically announce a deadline by which you will need to adopt the required amendment. This deadline will normally be the last day of the second calendar year that begins after the IRS lists the change on what the IRS calls the “Required Amendments List.”

But what about amendments that are not required because of a change in the law? Say, for example, you just want to change the design of your plan. In that case, you generally must adopt your amendment by the end of the plan year in which the change is to become effective. Depending on the nature of the change, it may be necessary for your amendment to be adopted earlier. For example, if you were adding a 401(k) feature to a profit sharing plan, you would need to adopt that amendment before it becomes effective.

Some changes can’t be made at all, at least with respect to existing plan contributions. It could be that the amendment would be to the disadvantage of participants. Say, for example, your plan allows terminated employees to take their money at the time they leave the company, even if they are young. And let’s say you want to change this so that participants cannot take their money until they are 65. You could not make this change with respect to money already in participants’ accounts. Participants would have a right to continue to take the money already in their accounts when they leave, even if they are under 65. But participants’ ability to take distributions before 65 could be eliminated for future contributions.

In some cases, changes cannot be made even with respect to future contributions. For example, if you want to lengthen the vesting schedule for matching contributions, requiring participants to work longer before they vest, you could not lengthen the vesting schedule for certain long-term participants, even for their future contributions.

NONDISCRIMINATION REQUIREMENTS

Among the tax code many requirements for qualified retirement plans are rules prohibiting your plan from favoring higher-paid employees. One thing these rules prevent is covering a group of employees having an overconcentration of highly compensated employees. These nondiscrimination rules also restrict your company’s ability to make larger contributions on behalf of, or to otherwise favor, highly compensated employees. The tax code even includes rules prohibiting your highly compensated employees from making contributions from their own pay at a rate that is too much higher than the rate at which your lower-paid employees contribute.

The constraints on the rate at which highly compensated employees make pretax contributions from their pay to 401(k) plans are determined by the “actual deferral percentage,” or “ADP,” test. You can avoid this ADP test by adopting a “safe harbor” plan design. Under a safe harbor design, your company would commit to making a minimum contribution for each covered employee or make matching contributions at a minimum level specified in the tax code.

Generally, the higher-paid employees who must not be favored under your qualified plan are those who earn above a specified annual compensation level. That compensation level for 2019 is $120,000 in preceding year compensation, but this threshold is adjusted annually for inflation. However, when inflation is low, the threshold may not go up.

IRS Audits

The IRS may audit your retirement plan, to determine whether your plan complies with the tax code. These audits will often be separate from your company's general corporate (or other business) audits. They are handled by specialists who are knowledgeable about the complex retirement plan rules. If the IRS finds errors, the consequences can be serious for your plan, your company, and your plan participants.

If it finds errors, the IRS may offer you an opportunity to correct those errors. If corrections are allowed, the IRS will probably require that your company pay a sanction amount. This would be on top of the cost of correcting the errors themselves. This sanction amount can be sizable.

CORRECTING ERRORS PRIOR TO AN IRS AUDIT

Sometimes, you will, on your own, discover an error relating to a qualified retirement plan. This could be a mistake in the plan document itself. More often, though, it will involve a failure to operate the plan correctly, such as by failing to follow the terms of the plan document. If this happens, the IRS offers a rather comprehensive and flexible program under which you may correct most errors related to qualified retirement plans.

> The IRS offers a comprehensive and flexible program for correcting qualified retirement plan errors, including mistakes in the plan document and failures to follow the terms of the plan document. Under certain circumstances, you may be able to correct errors without contacting the IRS or paying any fee.

EMPLOYEE PLANS COMPLIANCE RESOLUTION SYSTEM (EPCRS)

Under this IRS program, you may be able to correct certain plan failures without contacting the IRS or paying any fee. This ability to correct without contacting the IRS is the "Self-Correction Program" portion of EPCRS.

VOLUNTARY CORRECTION PROGRAM (VCP)

In many circumstances, the Self-Correction Program will not be available and it will be necessary for you to make an application to the IRS requesting permission to correct an error. In that event, you will describe in your application to the IRS how you propose to fix the error.

If you submit a correction application to the IRS, you will be using what is called the "Voluntary Correction Program" (VCP) portion of the EPCRS. The "fix" you propose will generally need to be consistent with correction guidelines set forth under the EPCRS.

The most common errors submitted to the IRS for correction under the VCP include:

- late plan amendments required by tax law changes
- not accurately following the plan's definition of "compensation" in determining contributions
- not including employees in the plan who should have been included
- including employees in the plan who should not have been included
- not accurately following the plan's loan provisions
- permitting withdrawals to participants while they are still employed when the plan does not permit those "in-service" withdrawals
- not properly making required distributions at age 70½
- not limiting 401(k) contributions as required under the ADP/ACP nondiscrimination tests
- failing to follow the "top heavy" plan rules that apply when certain owners and officers of the employer have at least 60% of the plan assets in their accounts
- not limiting contributions to the annual maximum permitted under the tax code

If you apply to the IRS for approval to correct an error, you will need to pay a fee to the IRS. If the IRS agrees with the proposed correction, it will issue a written "compliance statement" approving the correction. Importantly, you may not file a VCP application asking the IRS to approve a plan correction once you have received notice of a retirement plan audit by the IRS.

The fee you pay to the IRS under the VCP correction program is typically much smaller than the sanction your company would be required to pay if the IRS were to discover errors during an audit. As a consequence, many employers find it advantageous to voluntarily correct errors utilizing the IRS's EPCRS program. Making corrections under the EPCRS program only resolves those errors with the IRS and the federal tax code. The IRS can provide no assurance with respect to your plan's compliance with ERISA's non-tax code requirements. In some cases, ERISA includes provisions that are identical to those in the tax code.

Receiving a compliance statement from the IRS through the VCP does not assure that plan participants or the Department of Labor (DOL) will not raise a complaint under ERISA concerning the same error.

> The fee you pay to the IRS under the VCP correction program is typically much smaller than the sanction your company would be required to pay if the IRS were to discover errors during an audit.

FORMS 5500

A variety of reporting and disclosure requirements apply in connection with retirement plans. For qualified retirement plans, such as 401(k) plans, ESOPs, and qualified profit sharing and money purchase pension plans, the plan administrator must file an Annual Return/Report each year with the IRS and DOL on Form 5500. Small plans (generally, those with fewer than 100 participants at the beginning of the plan year) may be eligible to file the shorter Form 5500-SF instead of the regular Form 5500. Whether your plan will be eligible to file this shorter form will depend on whether it meets a variety of requirements described in the instructions for the form.

The Form 5500 for a plan year is generally due by the last day of the seventh calendar month after the end of the plan year. Your plan normally may obtain a one-time extension to file its Form 5500 (of up to two-and-one-half months) by filing Form 5558 with the IRS.

You must file this request for extension on or before the normal due date (not including any extensions) of the Form 5500. You must keep a copy of the completed Form 5558 requesting the extension with your plan's records.

> One of the most significant reporting and disclosure requirements applicable to qualified plans is the Annual Return/Report (Form 5500), which must be filed each year with the IRS and DOL.

PLAN AUDIT

As a general rule, if your plan has at least 100 participants, it must be audited each year by an independent, qualified public accountant. This audit must be attached to the Form 5500 that you file for the year. There is an exception to the audit requirement for small plans. This exception generally applies if your plan has fewer than 100 participants at the beginning of the plan year and meets certain other requirements. In some circumstances, a small plan that has grown to have at least 100 participants, but that still has no more than 120 participants at the beginning of the year, may retain its ability to file a Form 5500-SF, rather than a full Form 5500, and may be able to avoid the need for a plan audit.

The DOL has in recent years given special scrutiny to the quality of plan audits. The DOL has found that, in general, certified public accounting firms that handle relatively few employee benefit plan audits tend to make more mistakes in their audits. Because of this, the DOL has said that when engaging an auditor, you may wish to obtain references and discuss the auditor's work for other employee benefit clients. And the DOL has also suggested carefully reviewing the engagement letter with your auditing firm before the audit work begins. This letter should describe the audit work to be performed, the timing of the audit, and fees.

Once an audit has been concluded, the DOL suggests that you make sure the auditor, when preparing the audit report, has considered the following areas:

- whether the plan assets covered by the audit have been fairly valued
- whether plan obligations are properly stated and described
- whether contributions to the plan were received on time
- whether benefit payments were made in accordance with the plan's terms
- whether issues were identified that may impact the plan's tax-qualified status
- whether transactions prohibited under ERISA were properly identified

ACTION ITEMS

Develop a compliance plan to keep track of the various deadlines throughout the plan year.

Periodically review the plan documents to ensure that they reflect current practices and have been updated for legal and regulatory changes.

Ensure the completion and filing of all required government reporting, such as the Form 5500.

Ensure compliance with the applicable Internal Revenue Code nondiscrimination tests.

Review the process for collecting employee contributions and loan repayments, forwarding contributions and loan repayments to the service provider, and investing the contributions and loan repayments.

RESOURCES AVAILABLE AT T. ROWE PRICE

Annual nondiscrimination testing services—include projections of data to predict year-end results.

Form 5500 preparation—available through the Form 5500 service provider, Deloitte Tax LLP; includes the preparation of the Form 5500 and associate materials. There is no additional charge for this service.

Compliance calendar—includes important deadlines and details.

TRP preapproved volume submitter plan—has flexibility to customize certain features, aligns to best practices, and is preapproved by the IRS.

T. Rowe Price would like to recognize John L. Utz for his contributions to authoring this chapter.

JOHN L. UTZ

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ERISA 401(k) plans have moved from a supplemental to a central role in providing retirement income—indeed, it is now quite common for employees to rely only on a 401(k) plan to fund their retirement. And through tax deferral and opportunity for investment, 401(k) plans have become very popular vehicles for employees to fund retirement.

Fiduciary Liability and Threat of Private Litigation

This important role for 401(k) plans, however, has put increased pressure on plan performance, and has led to increasing ERISA-based litigation challenging the 401(k) plan fees and the selection of the mutual fund and like investments offered in the plans. Equally significant, ERISA can impose personal liability on fiduciaries for losses caused by fiduciary breaches including, in certain circumstances, breaches of co-fiduciaries. There also have been recent large attorney fee awards, which can encourage plaintiff's firms to take hard looks at plans to determine whether to bring litigation: **an August 2015 article noted that the law firm (Schlichter) that started bringing many of the ERISA fee lawsuits beginning in 2006 has collected $70 million in fees to date.**[1]

Plaintiffs in the fee cases probe for liability in *any* weak part in plan management and administration, even if the 401(k) plan is overall collectively sound and well managed. ERISA class action cases continue to be filed, including ones asserting new theories of liability.

The increasingly important role for 401(k) plans has put pressure on plan performance, and has led to increasing ERISA-based litigation challenging 401(k) plan fees and the selection of investment options.

[1] Diana Barr, Schlichter, Boeing settle 401(k) suit, ST. LOUIS BUSINESS JOURNAL (Aug. 27, 2015), http://www.bizjournals.com/stlouis/morning_call/2015/08/schlichter-boeing-settle-401-k-suit.html ("Eight settlements negotiated by Schlichter have produced more than $214 million in payouts, including $70 million for Schlichter, 67, and his firm, according to the Journal.").

Case Examples

Much of the litigation involving 401(k) plans has challenged their fiduciary management. The best and first line of defense for a fiduciary is to have a documented, prudent process supporting the decisions made.

> Engaging in a prudent fiduciary process is your best line of defense—instead of having to show, after-the-fact, that a prudent fiduciary would have come to the same decision.

For example, investments options should be reviewed periodically, including documenting the decisions and reasons to continue or discontinue the investment. The same need for review applies to retention of service providers for the 401(k) plan. The U.S. Department of Labor has made clear that although cost is a factor, a fiduciary is *not* required to accept the lowest cost provider. Rather, as part of proper fiduciary decision-making, you can and should consider quality and service (and any other factors relevant under the circumstances) in evaluating and retaining any service provider.

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Some of the relevant issues that have arisen in the cases include:

INVESTMENTS IN EMPLOYER STOCK

In a plan with a unitized stock fund (a fund holding stock and cash, with employee's investments based on unit values), a court allowed to go to trial claims that (i) the fund held excessive cash that caused investment returns to be depressed, and (ii) some participants' excessive in-and-out trading drove up the costs of the fund for other participants. The court criticized the fiduciaries for not having a prudent process investigating these issues.

Another recent case involving stock of a former employer that was spun-off illustrates the importance of having a prudent fiduciary process. The decision in that case—to close the stock fund of the spun-off company—plainly would have been prudent if supported with a prudent process. But because there was no evidence of a prudent process, the case was set for trial, with the burden on the fiduciary defendants to show that a prudent fiduciary would have come to the same decision to sell the fund.

RECORDKEEPING FEES

Plaintiffs have brought several claims challenging fees paid to record-keepers for the 401(k) plan, the vast majority of which plaintiffs lost. But plaintiffs have had some success when they have been able to show that the 401(k) plan fiduciaries have not periodically monitored these fees, e.g., asset-based fees will rise as the plan grows. There is nothing inherently improper about asset-based fees. Rather, the important point is that the plan fiduciary periodically monitors those fees to ensure reasonableness in relation to the services provided.

INVESTMENT FEES

Plaintiffs also have brought various claims challenging the fees paid for investments. Again, the vast majority of these claims have failed, e.g., courts have made clear that additional fees required to actively manage funds are not inherently imprudent. Courts have also not found revenue sharing to be improper, provided fiduciaries understand and monitor the fees involved and make reasoned decisions. Courts have found potential liability when fiduciaries may have incurred needless expense, such as by failing to evaluate whether there may be less expensive share classes available for the larger plan investor (such as institutional share classes) that offer the same mutual funds, but for less costs.

INVESTMENT SELECTION

In recent litigation, plaintiffs have brought variants of claims challenging the quality of various investments offered in 401(k) plans:

"Too aggressive"

In one case, plaintiffs challenged customized target date funds that included investments in hedge funds, private equity and commodity funds, all of which included higher than typical investment management fees and, in hindsight, had not performed well.

"Too conservative" or "good but not good enough"

In other cases, plaintiffs have challenged the offering of money market instead of stable value funds, or have challenged the investment makeup of stable value funds as being too conservative, and offering lower returns.

Courts are generally diligent about not judging investment claims with hindsight. But these claims do illustrate that all aspects of investment selection can be subject to scrutiny, and that it is important to have a prudent fiduciary process in place to defend investment decisions, instead of having to show, after-the-fact, that a prudent fiduciary would have come to the same decision.

CONFLICTS

Courts also consider whether there are any potential conflicts between the interests of the 401(k) plan participants and the company. In a case illustrating that even good intention can create risk, the company, not the 401(k) plan participants, paid the administrative fees of the plan. This created the potential for conflicts however because revenue sharing payments, which decreased the investment returns of plan participants, were used to lower the administrative costs paid by the company. Fortunately, after a trial, the court ultimately found that there was no actual conflict because it found that the revenue sharing payments did not motivate the selection of the investment options at issue.

Although focusing on areas generating risk of liability can be instructive, it bears noting that plan fiduciaries have won the majority of claims brought. These wins also can be instructive. For example, in one case a court dismissed claims challenging the selection of a money market fund because the plan fiduciaries had followed a prudent process. They had:

- Researched and compared the fees of four comparable funds;
- Reviewed the comparable funds (including fees) of seven candidates that responded to a request for proposals;
- Consistently monitored the fund's performance net of fees, which revealed that the fund performed consistently well (net of fees) throughout the period at issue;
- Periodically reviewed the reasonableness of the fees, which were reduced several times in the period at issue; and
- Conducted an extensive review of the fund in the period at issue.

Practices That Can Mitigate Litigation Risk

There are some general practices that plan fiduciaries should consider in managing and administering a 401(k) plan. As the cases teach, engaging in a prudent fiduciary process is your most important line of defense.

> It is just as important for you to document the prudent process that leads to the fiduciary decision at issue. This is critical for defending actions in court or before the U.S. Department of Labor, and to avoid having those decisions second-guessed with hindsight.

In selecting, evaluating, and retaining service providers—already stated on p.46—the cases suggest that the following factors are important:

- That plan fiduciaries understand how the service provider is compensated, and how much the service provider is earning, including from revenue sharing or any other form of indirect compensation.
- That plan fiduciaries periodically monitor the service provider's fees, and compare them against benchmarks or otherwise acquire information to confirm that they are reasonable, including factoring in service and quality.

Again, the U.S. Department of Labor has made it clear that you do *not* have to go with the lowest-cost provider, but it is important that you properly document this prudent fiduciary process and decision-making. In one case the 401(k) plan fiduciaries extensively discussed the matter at issue—i.e., whether to keep the employer stock fund unitized. The court suggested, however, that this did not show procedural prudence since this discussion did not result in any documented decision (continued unitization was not deemed to be sufficient evidence of a decision).

It is also a sound practice for you to periodically monitor all investments in the 401(k) plan, on both performance and fees. This includes when the fund is first selected and, as the cases make clear, in ongoing periodic reviews. Some other practices that may lessen risk for you in areas that have generated litigation include:

- Investigate and compare features, risks and costs of different investment vehicles as plan assets grow (e.g., funds (different share classes) to common trusts to separate accounts).
- If the plan uses unitized funds for employer stock or other investments, investigate and document your decision on why the plan is using a unitized approach for a fund.
- If it becomes apparent that certain plan participants are driving up plan costs through excessive trading, consider putting in place rules to reasonably limit trading.
- If the plan is closing down a fund or mapping investments from one fund to another, as a plan fiduciary you should document the reasons for this change, including why you selected the new fund over the prior one.

Finally, a practical way to lessen risk regarding plan investments is to offer a mix of diversified investment options, including target date funds for plan participants that do not want to manage their investments. A prudent process documenting that a plan fiduciary offered a diversified mix of investments can be a powerful rebuttal to hindsight-based claims that certain funds cost too much and performed relatively poorly.

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Preparation for a DOL Audit or Investigation

The U.S. Department of Labor's (DOL) Employee Benefits Security Administration (EBSA) has more than 300 investigators in 10 regional offices across the country that focus on ERISA plans. The DOL has broad powers to subpoena records and compel personnel to testify. The DOL can bring suit in federal court as well, which can include claims to recover monetary losses or disgorge profits, and for civil penalties and injunctive relief.

The DOL has responsibility for over 700,000 retirement plans. Accordingly, the DOL has to focus and prioritize its investigative and enforcement resources, including through national enforcement initiatives. Several of the DOL's enforcement initiatives are relevant to companies and fiduciaries for 401(k) plans. Some of the major areas investigated include:

- Timely and accurate depositing of employee contributions into the 401(k) plan.
- Compliance with ERISA's reporting and disclosure requirements, including ensuring that participants receive their statements timely.
- Compliance with ERISA's fidelity bonding requirements (discussed in the next section).
- Timely and accurate filing of Form 5500s.
- Whether there are potential conflicts of interest regarding plan investments.

The DOL also can make criminal referrals to the U.S. Attorney for, e.g., embezzlement of plan funds or intentional false statements in ERISA documents, such as the Form 5500. Other relevant areas commonly investigated include:

- Review of fees and expenses paid and plan investments offered.
- Review of investments in employer securities, and in any alternative investments.

> The DOL routinely investigates plans for compliance with ERISA, and approximately two-thirds of DOL investigations result in some form of monetary or other remedy.

The DOL routinely investigates plans for compliance with ERISA, and the fact that a plan is being investigated does *not* mean that the DOL believes there are violations of ERISA. However, approximately two-thirds of DOL investigations result in some form of monetary or other remedy, and certain factors are likely to trigger investigations, such as:

- Participant complaints.
- Inaccurate or inconsistent information on the Form 5500.

If you find errors or mistakes, there are actions you can take *before* the DOL initiates an investigation. The Voluntary Fiduciary Correction Program allows plan administrators to take corrective action to remedy the fiduciary breach and report the violation to the DOL, without requiring an enforcement action. The Delinquent Filer Voluntary Correction Program encourages plan administrators to bring their plans into compliance with ERISA's Form 5500 filing requirements by paying reduced penalties for late filings.

If the DOL has initiated an investigation of your plan, there are several things you may want to consider to protect your interests and facilitate the resolution of that investigation:

- Designate a point person (often an in-house or outside attorney) to coordinate and work with the DOL on the investigation.
- Consider notifying any fiduciary insurance carrier (ERISA fiduciary insurance is discussed in the next section) of the investigation.
- Discuss with the DOL investigator the documents requested to address the DOL's concerns while narrowing and focusing any broad requests, and develop a reasonable timeline and logistics for a response.
- Have an attorney prepare the interviewee and attend any interviews with the DOL. These interviews can be every bit as important as depositions in major civil litigation.

At the end of the investigation, the DOL typically sends a letter. A closing letter can conclude that no violations were found, or that the violations were minimal or have been adequately addressed. However, if the DOL believes corrective action is needed, it typically will send a voluntary compliance letter that will state the violations found and invite discussions to correct the violations. The DOL retains the right to sue, and may do so if exigent circumstances demand it or if there is no amicable resolution resolving the DOL's concerns. Voluntary compliance can avoid the 20% penalty imposed if the DOL sues and obtains a judgment or settlement on the challenged item.

ERISA Fiduciary Insurance and Fidelity Bonding Requirements

ERISA FIDELITY BONDS

Subject to certain exemptions for banks, insurers or broker dealers, ERISA imposes certain mandatory bonding requirements. If you are the plan fiduciary, you are responsible for ensuring that these bonding requirements are met both for yourself and for any (non-exempt) service provider who handles plan funds. Because the bond (often called a fidelity bond) is to protect the plan, the plan may pay for the costs of the bond.

ERISA requires every fiduciary and every other person (including non-exempt service providers) who "handle" funds or other property of the plan to be bonded. The fidelity bond protects the plan if the fiduciary or person handling the property or funds causes the plan to lose property through fraudulent or dishonest acts. The fidelity bond may name specific individuals or list specific positions, or be a blanket bond that includes all of the insured's officers and employees.

Some of the specific rules applicable for the fidelity bonds include:

- "Handling" is read broadly to mean whenever there is a risk that the person could cause loss of the plan's property through fraud or dishonesty, e.g., not just physical contact, but through the power to control the funds. This would include plan administrative or investment committees with final authority over plan funds.
- The bond must be from a surety or reinsurer approved by the Department of Treasury (available at fiscal.treasury.gov/fsreports/ref/suretyBnd/c570_a-z.htm).
- The bond must be for at least 10% of the money handled by the applicable insured, with a minimum of $1,000 and a cap of $500,000 ($1,000,000 for plans that hold employer securities). The bond can be for more than these minimums.
- The plan must be a named insured or otherwise able to enforce its rights under the bond.
- Unless exempt (such as certain banks, insurers or broker dealers), every person who handles funds or other property of the plan must be bonded.

ERISA FIDUCIARY INSURANCE

Unlike fidelity bonding, fiduciary insurance is not required. It is often advisable to have this insurance, however. As discussed in this and other chapters, as a fiduciary you have substantial responsibilities. Equally significant, ERISA can impose *personal liability* on fiduciaries for losses caused by fiduciary breaches including, in certain circumstances, breaches of co-fiduciaries.

The Basic Rules:

ERISA prohibits a plan from excusing or paying for a fiduciary's breach of duties. The plan can pay for fiduciary insurance, but the insurance must include the right to recover against any fiduciary that has been found to breach his fiduciary duty.

The company typically may indemnify (i.e., pay for) a fiduciary breach, and a company or the fiduciary can pay for fiduciary insurance that does not include the right to recover against a fiduciary.

Many forms of insurance (e.g., Director and Officer's or Employment Practices Liability Insurance) typically *exclude* coverage for ERISA fiduciary claims. Accordingly, if you want to have coverage for ERISA fiduciary claims, it is important to review the insurance coverage to make sure you are covered either by a fiduciary rider or a separate policy. Common items covered and excluded in an ERISA fiduciary policy are:

- Included are breaches of fiduciary duties arising under ERISA and negligence in administration of a plan (e.g., inaccurate communications to a participant).
- Typically included are defense costs, settlements and judgments. Fines and punitive damages are typically excluded.
- Excluded are claims of dishonesty, fraud, criminal acts, or where personal gain is realized.
- Also excluded are benefits due under the plan.

Many items can vary by policy, and should be considered when acquiring a policy. Some key items include:

- Handling of claims for wrongful acts that occurred before inception of the policy or future claims resulting from current or past lawsuits.
- Fiduciary insurance policies are typically "claims made" policies—the policy covers claims made during the policy period, even if the alleged wrongful conduct occurred before that period. It is generally a sound practice to give the fiduciary insurer notice when the insured becomes aware of facts or circumstances that may lead to a claim.
- The amount of the deductible and whether defense costs reduce the policy coverage.
- Whether DOL or other agency investigations are covered for defense costs, and whether the 20% penalty applicable for court orders or settlement of fiduciary breach claims with the DOL is covered.

In conclusion, although ERISA prohibits a fiduciary from being excused for liability for a fiduciary breach, a properly designed ERISA fiduciary liability policy can provide fiduciaries with funds to defend themselves in any lawsuit or investigation, and protect them from having to pay for any losses.

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ACTION ITEMS

Does the plan have a well-documented prudent fiduciary process for decision-making? Does it include documentation that decisions were actually made?

Are plan fiduciaries sufficiently covered by liability insurance that protects them from the costs associated with litigation (including unfavorable judgements)?

RESOURCES AVAILABLE AT T. ROWE PRICE

Fiduciary Checklist—includes information one should consider to help ensure their plan is compliant; could help prepare for a potential audit.

T. Rowe Price would like to recognize Robert W. Rachal for his contributions to authoring this chapter.

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Robert's work has focused on complex ERISA litigation, and on advising fiduciaries and employers on ERISA fiduciary issues. He's written and spoken extensively on these issues and have assisted clients in the defense of numerous class actions under ERISA, including those challenging investments in and administration of 401(k) plans.

Doing What's Right for Your Participants

Congratulations! You've completed Fiduciary Guide, an overview of ERISA fiduciary responsibilities and duties—which courts have described as "the highest known to law." We hope this guide helps you better understand who is a fiduciary, their basic responsibilities, and the importance of a well-documented process for fiduciary decision-making. We also hope it helps you recognize that while you're not required to be an expert, it's important to seek help from experts when needed.

ERISA contains specific obligations relating to interactions between your plan and participants, but we hope that you will think about going beyond the basics by considering plan features (such as auto-enrollment) and services (such as participant education) that are intended to improve participant outcomes. While outcomes are not part of your fiduciary responsibility, remember that you are responsible for properly implementing and operating plan features, programs, and services.

We encourage you to continue to stay current and learn more about topics that are of special significance to your responsibilities.

Thank you again for your interest in a serious but important responsibility—safeguarding retirement security for you and your co-workers.

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For additional fiduciary tools and materials, visit rps.troweprice.com/planview.