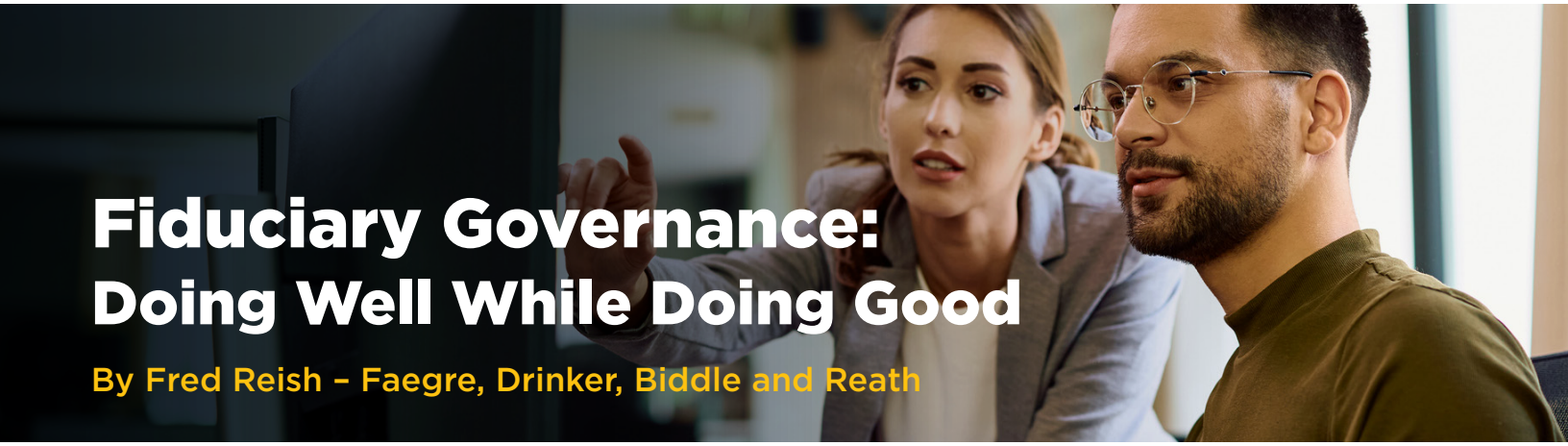

Fiduciary Governance: Doing Well While Doing Good

By Fred Reish – Faegre, Drinker, Biddle and Reath

Fiduciary governance is a fancy term for putting the right pieces in place to support compliance by plan sponsors with the fiduciary rules for operating retirement plans. It includes both adherence to the law to avoid fiduciary liability and adoption of best practices—which exceed the legal requirements—to both reduce risk and to improve outcomes for employees. Reducing risk is "doing well," while improving results is "doing good."

This article discusses some of the most import of the "pieces" for plan sponsors to put in place to manage risk and support participants in their financial journeys to retirement:

- **Knowing when you are a fiduciary.**
- **What does it mean to be a fiduciary?**
- **How fiduciary training helps with compliance.**
- **The basics of fiduciary "structure"—committee members, meetings and minutes.**
- **The role (and importance) of an investment policy statement (IPS).**
- **The role (and importance) of an investment adviser.**

Knowing when you are a fiduciary

The starting point is to ask, do you make decisions about the operation of your firm's retirement plan…about the service providers, the investments, the administration? If you do, then you are a fiduciary for making those decisions.

The most common decisions—and the ones that are often brought up in litigation—are the costs and quality of the investments and the compensation paid to the service providers. The officers and managers who make those decisions will either be appointed fiduciaries (for example, members of a plan committee) or "functional" fiduciaries—those that aren't formally appointed but make the decisions.

However, not every plan decision is a fiduciary decision. There is a concept of a "settlor"—the entity which sets up a plan. In making settlor decisions, officers and managers are not acting as fiduciaries. Settlor decisions include setting up, designing and terminating a retirement plan. The officers and managers who make those decisions are not fiduciaries and can act in the best interest of the company.

Several courts have made that distinction—between fiduciary and settlor—by pointing to a "two hats" doctrine. The courts say that an officer or manager of a firm can wear both a fiduciary "hat" and a settlor "hat"...but not at the same time. In other words, a settlor can design a plan for the benefit of the company, but when making decisions about the operation of the plan (for example, the investments or expenses), that same person must take off the settlor hat and put on the fiduciary hat...and act in the best interest of the participants.

What does it mean to be a fiduciary?

The law—ERISA, the Employee Retirement Income Security Act—places a number of responsibilities on fiduciaries. Some of the most important are to act:

- **For the purpose of providing retirement benefits for participating employees.** In other words, when making a decision about managing a retirement plan, fiduciaries should consider how the decision will favorably impact the retirement outcomes for the participants.
- **Ensure that the plan pays only reasonable expenses for its investments and services.** The requirement isn't that the cheapest investments or services be used, but instead that they be reasonably priced relative to what is available.
- **With the "care, skill, prudence, and diligence" that a knowledgeable person would use when making retirement plan decisions.** This means that fiduciaries must gather and thoughtfully consider the information that a knowledgeable person would consider when making a similar decision. If fiduciaries are not knowledgeable about a plan issue, e.g., mutual fund share classes, revenue sharing, reasonable provider compensation—they are obligated by ERISA to obtain expert advice.
- **To diversify a plan's investments.** For participant-directed plans, such as 401(k) and 403(b) plans, that means that the plans should offer a "broad range" of investments to participants. "Broad range" means that the options are varied enough that a reasonable person could put together a portfolio that reflects the person's risk and return needs. Fiduciaries may need the help of a knowledgeable adviser to determine the number and type of investments to be offered.
- **To follow the terms of the plan document.** While that seems straight forward, experience shows that plan sponsors do, on occasion, inadvertently fail to follow the document's provisions. An example is that a plan sponsor may report participant compensation to the providers that is not calculated in the same manner as the plan's definition of "compensation."

In addition to those components of ERISA's prudence standard, fiduciaries have a duty to be aware of and manage any conflicts of interest of their service providers. For example, it would be a conflict if a service provider makes a recommendation that would result in additional compensation for the service provider.

How fiduciary training helps with compliance

Fiduciary training is valuable for several reasons. For example, courts have pointed to fiduciary training in finding that fiduciaries were aware of and performed their duties. The training shows a degree of earnestness by the fiduciaries.

In addition, the law and court decisions impose a number of requirements on fiduciaries that may not be obvious. For example, the Department of Labor (DOL) has taken the position that fiduciaries have a duty to keep track of former employees who still have benefits in the plan. Similarly, the DOL has issued guidance on fiduciary responsibilities for cybersecurity. Also plaintiffs' attorneys often sue fiduciaries claiming that they selected overly expensive "share classes" of mutual funds. Those are just a few examples, but the message is that fiduciaries may not be able on their own to identify—and then assess—all of the issues they must address. Fiduciary training, updated each year, can help plan fiduciaries stay abreast of their responsibilities.

The basics of fiduciary "structure"—committee members, meetings and minutes

ERISA does not require that plan sponsors set up committees to be the fiduciaries for a plan; instead, it is a best practice. If a committee is set up, it should meet regularly and the members should engage in collaborative discussions to make decisions. That is what fiduciaries are supposed to do. The most common schedule for committee meetings is quarterly, although committees for smaller plans may decide to meet only twice a year.

A committee should be made up of officers and managers. It's important to have people who are used to receiving information and making important decisions based on that information. That is, in essence, what a fiduciary does.

A committee should have diverse membership….perhaps someone from finance, human resources, payroll…in order to have knowledge about the different issues that will come up.

As a best practice, committees should document their meetings. That is commonly done through minutes, but it could be a memo or other writing. The key is to document the meeting, who attended, what information was received, and what decisions were made (or deferred). Other than listing the attendees, there isn't a requirement to say which committee members said what, or who made the motions, and so on. The key, though, is for the committee to have real discussions about each issue. The minutes shouldn't suggest that decisions were made summarily.

In addition, if an adviser is at the meeting, the minutes should show that the adviser made recommendations and that the committee members asked questions to fully understand the basis for the recommendation. After all, the committee makes the decisions and the law says that fiduciaries cannot "blindly" rely on their advisers.

Maintaining written records of committee meetings, including any reports from advisers and providers, is important evidence of fiduciary compliance.

The role (and importance) of an investment policy statement (IPS)

An investment policy statement is not required by law—it is a best practice.

In effect, an IPS is a roadmap for the compliant selection and monitoring of a plan's investments. The IPS should be detailed enough that the committee can apply it when making investment decisions—and a committee would be well-served to ask their adviser how the adviser's investment recommendations comply with the IPS. However, the IPS should not be so detailed that it ties the hands of the committee members. The key is that committee members make thoughtful investment decisions for the benefit of the participants...an IPS should just be a support tool for that purpose.

An IPS should—as a best practice—be reviewed by the committee members once a year, so that it is fresh in mind when investment decisions are made. The IPS is also a useful training tool for new committee members.

As with some of the other points discussed in this article, courts will point to an IPS as evidence that fiduciaries were attentive to their duties.

The role (and importance) of an investment adviser

There was a discussion earlier in the article about how fiduciaries are measured by the standard of a "knowledgeable" person. In effect, the law says that fiduciaries don't have to be knowledgeable experts about all of the decisions they have to make, but where they are not knowledgeable, they must engage experts to help them. That is the role of an experienced retirement plan adviser.

There are several areas where fiduciaries commonly need help. For example, plan committees may need selecting reasonably-priced investments. But mutual funds and other investments may have multiple "share classes," each with its own expenses---but all are part of the same pool of investments. Which share classes are available to your plan (most often based on the total assets in the plan)? And, of those, which is the most favorably priced for your plan, taking into considerations of revenue sharing and other factors? Those are questions for experienced investment people and may be beyond the knowledge of the plan committee members.

Another key issue is the total compensation of a plan's recordkeeper, including both direct and indirect payments. For example, does your recordkeeper receive revenue sharing from the plan's investments? If so, did you consider that in benchmarking the total compensation of the recordkeeper relative to its competitors?

It is difficult to navigate the fiduciary waters without help. That is the role of a retirement plan adviser...and courts have commented favorably where plan committees have used advisers.

Concluding thoughts

Plan fiduciaries need to make decisions that are in the best interest of their participants. The context for "best interest" is the retirement security of the participants. Paying too much for plan services and investments can violate that standard because it will reduce the amount on money that the participants have for retirement.

Having a good infrastructure for identifying the necessary decisions and how to best make them is critical. Fiduciary training, committee meetings and an IPS are helpful tools in making the needed decisions in the right way.

However, some of the decisions are complex and involve considerations that committee members may not be familiar with. That's why an experienced adviser can be invaluable—both for legal compliance and best practices.

By having the right pieces for the fiduciary puzzle, plan committees can have a smoother path to fiduciary compliance. That is the essence of fiduciary governance and of "doing good while doing well."

This content was authored by Fred Reish. Fred Reish is a partner with the law firm of Faegre Drinker who specializes in retirement law, focusing on fiduciary and best interest standards of care, prohibited transactions, conflicts of interest, and retirement plans.

RPW-347-0424 (Exp. 04/26)