PLAN GOVERNANCE –
DO’S AND DON’TS

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Kathleen Odle, Esq.
Sherman & Howard L.L.C.
303.299.8116
Why is Governance Important?

An effective plan governance program will:

- Simplify and streamline decision making
- Reduce risk for the plan and its fiduciaries (which reduces exposure for the company)
- Increase the likelihood that plan and participant objectives are met
- Save time when a new committee member is appointed or when information about the plan is requested in an audit of the plan
Consider These Questions to Determine if your Plan Governance is Adequate

- If you asked everyone involved in the operation of your retirement plan what their duties and responsibilities are, would you get the correct answers?

- If there were a change in the people providing services to your plan, would the existing documentation allow for new personnel to transition easily into their roles?

- In the event of an IRS or Department of Labor audit, would you be able to supply information quickly about who is responsible for doing what?
All authority over a retirement plan starts with the Plan Sponsor. The Plan Sponsor then can delegate certain powers to other people.
Authority Over Plan

Who approves the plan?

- If the Plan Sponsor is a corporation, the Board of Directors of the corporation would approve the plan.
- If the Plan Sponsor is a partnership, the managing partner would approve the plan.
- If the Plan Sponsor is a limited liability company, the person(s) with management authority over the LLC (check the LLC operating agreement) would approve the plan.
Authority Over Plan

When adopting a new retirement plan, the Plan Sponsor will usually appoint:

- the trustee
- the recordkeeper/TPA
- other service providers

The Plan Sponsor also can establish a committee and delegate powers to the committee, or the Plan Sponsor can retain certain powers.
One Type of Arrangement

Corporation ABC Adopts a 401(k) Plan

The Board of Directors of Corporation ABC Establishes a 401(k) Plan Committee and Delegates to the Committee full power and authority over the Plan

The Committee now has the authority to appoint the recordkeeper/TPA, to amend the Plan, to monitor investments, and to act as Plan Administrator for the Plan
Delegation of Authority

- Authority must be delegated from the Plan Sponsor to any person or committee – a person or committee has no authority without delegation from the Plan Sponsor.

- Where do you find a delegation of authority?
  - (a) Plan Document
  - (b) Board Resolutions
  - (c) Committee Charter or Committee Bylaws
Zelda finds out that she has been appointed to the 401(k) Committee at her employer. She wants to know what her responsibilities will be as a 401(k) Committee member.

Who should she ask?
Challenge Question #1 - Possible Answers

Possible Answers:

(a) The head of HR

(b) The company’s lawyer

(c) The president of the company
The person who “takes charge” of arranging for the orientation of new Committee members can be anyone at the company, but there should be some process in place where new Committee members receive relevant documents and education about their duties.
Summary - Delegation of Authority

• DO review all applicable documents to determine who has authority over the plan, and the extent of that authority

• DON’T assume that the committee members can sign any document relating to the plan

• DO “fill in the gaps” if you cannot locate proper delegation authority – it is better to document your delegation process now than to continue to operate without proper delegation

• DON’T assume that the delegation has been done properly just because the plan has been in existence for many years
Orientation and Education of Committee Members

- Members of a plan committee should be provided with:
  - the plan document
  - the plan’s summary plan description
  - the plan’s investment policy statement
  - the committee’s charter or bylaws, if any
  - any other delegation of authority
  - any other document that addresses the committee’s duties
  - information about fiduciary insurance coverage, if any
Orientation and Education of Committee Members

- Members of a plan committee should also:
  - accept their appointment to the committee in writing
  - receive fiduciary education
    - this can be a short seminar on fiduciary duties and can be provided by the plan’s investment advisor or ERISA attorney or the committee member can attend a publicly available fiduciary education program
Ongoing Education for Committee Members

- Even where a committee has been in place for a period of time, the committee should receive ongoing fiduciary education.

- A quality investment advisor will keep the committee up to date on changes in the law regarding fiduciary duties, and would provide these updates with their regular investment reports.

- Committee members should consider attending (either in person or via webinars) professionally produced fiduciary seminars (such as this one!)
Ongoing Education for Committee Members

- There are publications that can assist in keeping committee members informed about the ever-changing landscape of laws applicable to retirement and other benefit plans
  - Plan Sponsor Magazine
  - Publications from companies that provide fiduciary advice
- Many ERISA lawyers publish periodic client advisories on legal changes impacting retirement plans
  - You do not need to be a client of the law firm to receive these client advisories
Document Your Fiduciary Education Efforts

- The Department of Labor has begun to ask about fiduciary education in their audits of retirement plans.

- Being able to provide documentation on education efforts (such as this seminar!) shows the DOL that you take your fiduciary duties seriously.
Summary - Fiduciary Education

• DO provide fiduciary education for your committee members and keep records of that education
• DO consider education for your non-fiduciary employees who deal with retirement plan matters
  – i.e., payroll personnel need to be educated on the importance of following proper payroll procedures
• DON’T assume that your committee members understand how the plan operates
• DON’T assume that your committee members are sophisticated investors
  – Committee members should be educated on the different reports, charts and graphs provided by the investment advisor
Committee Duties

• Committee duties can be divided into two categories:
  – Settlor functions
    • Power to amend plan, terminate plan, etc.
    • Committee acts on behalf of the Employer, not Plan Participants
  – Fiduciary functions
    • Fiduciary functions include selecting/monitoring investments available under plan, hearing and making determinations on claims and appeals, application of plan terms, selection and monitoring of plan service providers (TPA, trustee, investment advisor), interpreting plan provisions
    • Committee acts on behalf of the Plan Participants, not the Employer
Committee Duties

• Remember, not all committees have authority over settlor functions
  – Some committees only have authority over the plan’s investments, which are fiduciary functions

• It is important to recognize the scope of the committee’s authority
# Settlor Functions vs Fiduciary Functions

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<thead>
<tr>
<th>Overview</th>
<th>Settlor Functions</th>
<th>Fiduciary Functions</th>
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<tbody>
<tr>
<td>Company and/or business related decisions which are not subject to a fiduciary standard of care</td>
<td>Subject to a higher standard of care because fiduciary acts on behalf of plan participants</td>
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**General Responsibilities**

<table>
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<tr>
<th>Settlor Functions</th>
<th>Fiduciary Functions</th>
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| Mostly plan design related:  
  • Establishment of plan  
  • Level of benefits provided  
  • Plan amendment and termination | Mostly plan governance related:  
  • Act solely in interests of plan participants  
  • Act with exclusive purpose of providing benefits to participants  
  • Carry out duties in prudent manner |
Challenge Question #2

Question

The Board of Directors of Company Clueless isn’t scheduled to meet anytime soon and the TPA says that an amendment to the 401(k) plan must be signed NOW. The Plan Investment Committee for the 401(k) plan decides to approve and sign the amendment. Is this OK?
Possible Answers:
(a) Of course, don’t all committees have the right to amend the plan?
(b) No, an investment committee never has authority to amend the plan.
(c) The committee should check its charter or other delegation of authority to determine its authority.
Challenge Question #2 - Correct Answer

Correct Answer:

(c) - The powers and authorities of a committee are set forth in the committee's charter or other document (such as Board resolutions) that delegates authority to the committee. If there is no delegation of authority to sign plan documents and amendments, the committee does not have that authority.
Summary - Settlor vs. Fiduciary Functions

• DO know the extent of the committee’s authority and what documents and actions the committee can approve

• DON’T assume that any company officer has the authority to sign any document relating to the plan

• DO ask for documentation from the governing body (i.e., board of directors, managing partner, etc...) if you cannot determine whether authority has been properly delegated

• DON’T be stonewalled by upper management – this is important for reducing risk to the company
Governance Procedures

Create Procedures

Review the Procedures

Follow the Procedures

Document all Decisions
FIDUCIARY DUTIES

• Each fiduciary should be aware of the scope of his/her duties under the plan.
  – Duty of loyalty (exclusive benefit rule)
  – Duty of prudence ("prudent expert" standard)
  – Duty to diversify
  – Duty to follow plan terms

• Courts are not kind to fiduciaries who claim not to have known about their fiduciary duties.
DECI SI ON MAKING PROCESS

• Courts in ERISA fiduciary breach cases have consistently stated that the fiduciary does not need to be “right” on every decision, but that the decision making process is what will determine fiduciary liability.
  – It is not the result, but the process of making the decision that the court reviews.
  – By being able to demonstrate that the fiduciary engaged in prudent due diligence before taking any action, fiduciary liability can be avoided.
DECISION MAKING PROCESS

INVESTMENT MONITORING AND INVESTMENT POLICY STATEMENTS

- ERISA does not require that an Investment Policy Statement (IPS) be adopted for a plan.
  - IPS can be a valuable tool to document the committee’s decision making process in selecting and monitoring investment options.
  - IPS also can be used as a tool to prove a breach of fiduciary duty if the fiduciaries do not follow the IPS in all respects.
  - An IPS should not lock a committee into any required action, unless the committee is ready to take that action.
SELECTED AND REVIEW OF INVESTMENT OPTIONS

• Meet and discuss investment options regularly
• Record decisions in meeting minutes
• Report regularly to the Plan Sponsor (i.e., the board of directors)
• Review the fee structures of the investments and plan administration – compensation paid to every service provider must be *reasonable*
  – Comparison
  – Benchmarking
  – Requests for proposals
SELECTI ON AND REVIE W OF INVESTMENT OPTIONS

• Get professional help
  – ERISA requires that a fiduciary fulfill his/her duties in the same manner as a person “familiar with such matters”. This effectively imposes a “prudent expert” standard on plan fiduciaries.
  – Most plan fiduciaries need assistance with performance evaluations in order to meet their fiduciary duties. Unless the fiduciaries have investment experience, they may not be able to fulfill their duty to monitor the investments “prudently” without the aid of an investment advisor.
The Committee and the investment advisor should review:

- The performance of funds
- Expense ratios of funds (and, for the 401(k) plan, the resulting allocation of plan expenses to participants)
- Fee structure and revenue sharing

The Committee also has a duty to monitor the investment advisor.
SELECTED AND REVIEW OF INVESTMENT OPTIONS

• Pay attention to the investment review and ask questions
• Committee members should have a basic understanding of all of the information, charts, tables that are included in the investment review booklets
  – If education is needed on the investment reports that are provided to the committee, have the investment advisor do a special education session and document that session
Challenge Question #3

Question

The Investment Committee for the Company Clueless 401(k) Plan uses an investment advisor, and meets regularly with the investment advisor, but the Committee members don’t really understand the advisor’s reports or the advisor’s recommendations (although they always follow the advisor’s recommendations).

Does this raise any concerns?
Challenge Question #3

Possible Answers:

(a) Not a problem, as long as the Committee follows the investment advisor’s recommendations, they will be safe from liability.

(b) The Committee should fire the investment advisor.

(c) The Committee should ask the investment advisor for more assistance in understanding the reports and the advisor’s recommendations.
Challenge Question #3

Correct Answer:

(c) The Committee should understand their fiduciary duties and that simply hiring and following an investment advisor’s recommendations without understanding the advisor’s reasons for those recommendations does not satisfy their fiduciary duties.

Also, the investment advisor should assist the committee members in understanding the reasons for their recommendations.
Summary - Decision Making Process

DO establish and communicate who (or which group) performs each plan function

DO be prepared to demonstrate, after the fact, your plan governance and decision making process

DO set up good communications between all plan-related parties, including internal and external

DON’T ignore the information and tools offered by your plan’s service providers to help you fulfill your duties

DON’T just set your plan governance structure and forget it - periodically check how your plan governance structure is working and whether it can be improved
Steps to Take Now

• Gather your documents in one place and create an index of those documents

• Determine if there are documents that properly delegate authority over the plan’s operations
  – If so, confirm that you are following that process
  – If not, consider “redoing” everything… reappoint the committee, delegate authority to the committee, create a committee charter or bylaws that address the committee’s duties and authority, and educate the committee on those duties and authority
Conclusion

• Is it never too late to establish a solid governance program and to properly document that program
• There is not one perfect governance program
• Each company may approach governance and delegation of duties in different ways