FIDUCIARY BEST PRACTICES:

Taking a prudent approach to plan management

A White Paper Prepared by
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Taking a prudent approach to plan management

Employing a set of best fiduciary practices remains a core objective of plan sponsors, retirement plan committees, and trustees. The current economic environment, market volatility, participant-related lawsuits, declining retirement account values, and fee disclosure legislation have compounded the need for retirement plan sponsors and plan fiduciaries to seek out and implement fiduciary practices to maintain regulatory conformity and to shield themselves from personal liability.

To assist plan sponsors and fiduciaries, Transamerica Retirement Solutions has assembled a set of principles-based, prudent best practices that have become commonplace among retirement plans subject to the Employee Retirement Income Security Act (ERISA) of 1974, which is the American federal statute that establishes minimum standards for pension plans in private industry. A large part of satisfying ERISA fiduciary duties relies simply on identifying fiduciaries and having those fiduciaries follow certain procedures that will guide them in acting prudently, known as "procedural prudence." In this paper, we will present a summary of best practices that plan sponsors and fiduciaries can employ to ensure they are meeting their obligations.

Appointment of a fiduciary committee

The first essential step is to identify fiduciaries to administer the plan and oversee investment decisions. These appointments should be consistent with criteria outlined in the plan document. Though the fiduciary may be a single individual or the employer itself, a common best practice is to have several individuals on a plan committee who will divide up the duties. For large employers, there may even be separate committees–with one attending to administrative matters, such as overseeing employee communications and handling benefit claims, and another managing investment matters. The committee should be composed of personnel who are familiar with pensions and investments. Providing committee members with some periodic education on the plan's operation and on ERISA fiduciary duties is also considered a best practice.

Additional considerations

Some plans identify the employer as the named fiduciary while also providing that the specific fiduciary duties can be delegated, which is a common and practical approach for many employers. While it is permissible to do this, naming the employer does not necessarily make it clear exactly which individual(s) have fiduciary responsibility for the plan. For example, "the employer" may include board members and senior officers who are not aware of the implications of the role. Therefore, making appointments to a plan's fiduciary committee requires some thought. The goal should generally be to appoint individuals who will be making the actual decisions and thus will be in fact the fiduciaries. The idea here is that the best fiduciary decisions are made by people who understand their roles and what their duties entail. In addition, a committee should not consist of people too senior or too busy to fulfill these duties, nor those so junior that they do not have the authority to make independent decisions.

Written committee charter

In keeping with "procedural prudence," a committee should have a written charter outlining its organizational responsibilities (chairman, secretary, quorum, etc.), how it operates and decides matters, how it conveys its decisions to others (such as by the secretary), and how often it meets.

Periodic committee meetings

Once appointed, the committee should meet regularly. Once a quarter is common for most organizations, though special meetings may be held when warranted. The secretary or other appointee should keep minutes for each meeting, which will concisely cover all the important issues discussed.

Typical fiduciary structure for a retirement plan

Board of Directors

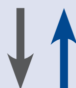
- Retains the strategic (non-fiduciary or "settlor") decision-making authority over the plan
- Approves material amendments and/or plan termination
- Fiduciary role is limited to delegating responsibility for the plan to the CEO

CEO

- Selects, monitors, and replaces retirement plan committee members

Retirement Plan Committee

- Typically composed of five or more members appointed by the CEO
- Charged with investment and administrative functions of the plan
- Approves all legally required amendments and non-material amendments
- Designates the CEO as the plan fiduciary

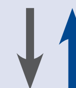


Plan Investment Functions

(retained by the retirement plan committee)

Functional activity:

- Select, monitor, and replace all of the investment options offered under the plan
- Appoint an independent investment advisor to be a fiduciary and to provide input on these decisions
- Determine all questions that arise concerning the construction and interpretation of the plan and the administration

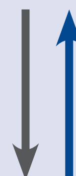


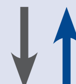
Plan Administrative Functions

(often delegated to human resources department)

Functional activity:

- Comply with all reporting and disclosure requirements to which the plan is subject
- Adopt such rules and regulations as reasonably necessary for the proper and efficient administration of the plan
- Direct recordkeeper on all matters involving eligibility for, account balances under, and distributions from the plan
- Appoint or employ individuals to assist in the administration of the plan





Independent Investment Advisor

The investment advisor (in his/her capacity as fiduciary) should provide information to evaluate the investment options and make recommendations regarding appropriate investment funds

Retirement Plan Custodian and Recordkeeper

Legend

Allocation and Delegation →

Reporting Back →

Investment policy statement

Creating an Investment Policy Statement (IPS) is an essential fiduciary best practice. The IPS serves to outline the criteria for selecting and monitoring the providers and investment options, without identifying specific investments. There is no standard form for an IPS, but a typical one will cover:

- Clear identification of the plan and the fiduciaries responsible for investments under the plan.
- Identification of the asset classes that are generally intended to be available under the plan (e.g., domestic large cap, domestic small cap, etc.).
- Selection criteria for a mutual fund or other investment to be added and/or removed from the plan, such as history, management, style, past performance, benchmarks, and fees.
- Ongoing investment monitoring criteria, such as which benchmarks to use and how to evaluate fees.
- Use of investment consultants.

Initial evaluation of investment providers and investments—the request for proposal process

Fiduciaries have a duty to prudently select investment providers and their underlying investments. Procedures for doing so in an organized and documented manner should be identified in the IPS. Although not mandated by ERISA, using a formal Request for Proposal (RFP) in order to evaluate and select providers and investments is a common best practice, especially for larger plans.

Meeting fiduciary obligations for a 403(b) plan

With the release of the final 403(b) regulations by the Internal Revenue Service (IRS) in 2007, 403(b) plan sponsors must now operate their plans much more like 401(k) plans. One of the most crucial considerations for a 403(b) plan sponsor, in light of the final regulations, is the personal exposure he or she has to the Employee Retirement Income Security Act, or ERISA. Sponsors of 403(b) plans and plan fiduciaries are quickly learning that failure to comply with ERISA can result in personal liability for any breach in compliance.

If an employer has not yet taken steps with its 403(b) plan to comply with ERISA, the time to do so is now. There is no question that audits and compliance efforts by the IRS and Department of Labor are ramping up. By not taking immediate action, any liability for past violations may only be compounded and extended to new fiduciaries. By taking action now, fiduciaries may be able to mitigate any exposure they may have.

Review Transamerica's *Avoiding the Breach: Bringing higher education 403(b) plans up to date with current ERISA fiduciary best practices* white paper for an in-depth explanation of best fiduciary practices for 403(b) plans.

Other considerations

An RFP process does not need to be overly complicated. It is important to keep in mind that its purpose is to elicit clear information from possible investment and service providers regarding the services they will provide to the plan, along with their fees and other costs. The RFP should provide prospective providers with the existing plan documents, the current Summary Plan Description (SPD), and other plan-related information so that they can properly understand the goals and objectives of the plan. The RFP should also be very clear about the scope of services the plan sponsor is seeking, for example, whether the vendor should provide both investments and administrative services (such as plan documents, SPDs, recordkeeping, distributions, testing for IRS contribution limits and non-discrimination testing, and preparation of 5500 forms) or whether the sponsor will consider respondents who provide only some of those services.

Evaluation of the RFP responses is the most critical step in the process. Fiduciaries should review responses from providers carefully and select the provider(s) that can offer products and services consistent with the needs of the plan.

Many sponsors elect to go through the RFP process with plan providers every three or five years in order to survey the market and ensure their plan is competitive. This may also be considered a general best practice.

Evaluating investment fees

The Department of Labor has been giving significant attention and has enacted regulations regarding fees charged by providers to participants and beneficiaries. Allegations have included fiduciaries not properly determining if their plan is obtaining services that are justified relative to the fees assessed by the plan's providers, and whether or not, as a fiduciary, they could have selected other comparable investments at a lower cost to participants. The controversy over "reasonable" fees for services rendered has underscored the importance of the fiduciary duty to understand the fees the plan is paying. Additionally, fiduciaries are expected to determine whether they can lower fees by obtaining comparable investments and services. Being aware of what fees are being paid (both directly and indirectly), taking them into account as a factor in making investment decisions, and documenting that process is considered a critical best practice for fiduciaries.

Monitoring investments

A fiduciary has a duty both to prudently select the provider and the investments that will be available under the retirement plan and to monitor those investments on an ongoing basis. As a best practice, the fiduciary committee should meet at regular intervals and compare the returns of the selected investments with their appropriate “benchmarks.” Benchmarks should also be prudently chosen and reevaluated from time to time. This process should be outlined in the IPS, with the committee keeping minutes of the meetings that address the issue. If there are any concerns about the performance of a particular investment, a change in management of the fund, or “style drift” (which occurs when a fund appears to move away from its original stated objectives and investment holdings), the committee should investigate and take appropriate action. In addition, the committee should be prepared to follow up to ensure that action has actually been taken. Any and all concerns addressed by the committee should be reflected in its meeting minutes.

Fund mapping, blackouts, and default investments

Though outside the fiduciary-specific focus of this paper, it’s worthwhile to note that ERISA provides guidance on a number of common transactions and decisions, and many providers have incorporated this guidance into their practices. Examples include fiduciary safe harbors arising out of the Pension Protection Act of 2006 when selecting “default investments” and the “mapping” of funds moved from one investment provider to another. ERISA also provides guidance on the regulations governing “blackout” periods, when the participants’ ability to make transactions is temporarily suspended, and governance on required participant notifications when monies are moved from one investment to another. Fiduciaries should consult with their providers and tax and legal advisors regarding such practices.

Best fiduciary practices for non-ERISA plans

Even if a plan is not subject to ERISA, such as a church or public college or university 403(b) plan, it is prudent for plan sponsors and fiduciaries to follow ERISA-like best practices voluntarily. In many states, there may be general fiduciary duties under common law or under statutes for charitable entities and certain public retirement plans. How and whether these rules might apply to a church or governmental 403(b) plan may be untested, but one does not want to be the test case. Therefore, being able to say “we performed to the same standard as if we were ERISA fiduciaries even though we are not” will be a much more defensible position should any litigation arise.

Step-by-step approach to meeting fiduciary obligations	
STEPS	**MISSTEPS**
Educate yourself on your role as a fiduciary and the scope of responsibilities you will have to the plan in this capacity.	Don't stop acting as a plan fiduciary without formally resigning or receiving written direction from plan authorities that you are no longer a plan fiduciary.
Make sure an ERISA bond is in place before taking any action on behalf of the plan; request a formal appointment by the plan before acting in any capacity on the plan's behalf.	Don't act on behalf of the plan without adequate coverage; procedurally, the ERISA bond should be reviewed annually to make sure the coverage is adequate.
Require indemnification from the plan sponsor for any direct or indirect liabilities.	Make no assumptions about what constitutes a fiduciary breach—ask for clarification from a trusted source and review how a breach could affect you.
Identify and document in writing all persons acting as fiduciaries on behalf of the plan. Organize formal periodic meetings among the plan's fiduciaries and other plan authorities; document these proceedings.	Limit written documentation to those details pertinent to the management of the plan; don't editorialize.
Outline the criteria and evaluation process to follow for any contracted third-party services. Contract for third-party services only after a thorough evaluation process has been completed and documented.	Do not fail to obtain a comprehensive service contract that outlines clear deliverables, timelines, costs, and liabilities assigned to the parties to the agreement.
Review the plan document to ensure it is consistent with ERISA requirements; correct any inconsistencies.	Don't forget to amend the document periodically to reflect plan changes.
Make certain the plan affords the fiduciaries discretionary decision-making authority.	Do not act in an impulsive or arbitrary manner.
Organize and maintain a complete set of all current documents, including Plan, Trust, Investment Policy Statement, Summary Plan Description, forms, and service agreements; institute a records retention policy.	Don't let documents become out of date; update them periodically to reflect any amendments.
Formalize investment policies and procedures.	Avoid making exceptions to written policies and procedures.
Ensure the plan provides comprehensive participant education and communication.	Avoid incomplete or inconsistent communications to plan participants that call for interpretation on their part.
Develop diverse investment choices for participants—emphasize investment selection in education curriculum so participants make informed choices.	Don't assume you have no liability for investment diversification under ERISA 404(c).
Monitor plan investments regularly to ensure acceptable continuous performance.	Do not simply add funds to existing underperforming funds; remove underperforming funds as necessary.
Devise strict administrative policies and remedies—especially claims procedures.	Do not make exceptions to these policies.
At all times act in the sole interest of the plan participants and beneficiaries.	Don't engage in self-dealing transactions or transactions where you or other fiduciaries have a self-interest or conflict of interest.

Conclusion

Plan sponsors and fiduciaries of ERISA retirement plans should not panic if they have not yet undertaken the steps described above as best practices. But neither should they expect to continue with the status quo. As employers grasp the implications of their fiduciary duties, they are rapidly moving toward compliance, determining who the fiduciaries are or should be, revising the plan document, and selecting and monitoring all providers. So it's important to have a carefully outlined approach for taking on that process.

Retirement plan sponsors may find that bringing their plans into full compliance means making some significant changes. Remember, what's most important is that fiduciary decisions are made in an organized manner with the interests of the participants and beneficiaries in mind. By following this basic principle, plan sponsors and fiduciaries can find their way toward the best solutions.

About Transamerica Retirement Solutions

Transamerica Retirement Solutions (Transamerica) is a leading provider of customized retirement plan solutions for organizations of every size.

Transamerica partners with financial advisors, third party administrators, and consultants to cover the entire spectrum of defined benefit and defined contribution plans, including: 401(k) and 403(b) (Traditional and Roth); 457; profit sharing; money purchase; cash balance; Taft-Hartley; multiple employer plans; nonqualified deferred compensation; and rollover and Roth IRA.

Transamerica helps more than three million retirement plan participants save and invest wisely to secure their retirement dreams. For more information about Transamerica Retirement Solutions Corporation, please visit **www.trsretire.com**.

Nothing presented herein is intended to constitute legal or investment advice, and no investment or plan design decision should be made solely based on any information provided herein. Nothing presented herein should be construed as a recommendation to purchase or sell a particular investment or follow any investment technique or strategy. Any forward-looking statements are based on assumptions and actual results are expected to vary from any such statements. While Transamerica has used reasonable efforts to obtain information from reliable sources, we make no representation or warranties as to the accuracy, reliability, or completeness of third-party information presented herein. Past performance is no guarantee of future results. There can be no assurance that any particular asset class will outperform another asset class. There is a risk of loss from an investment in securities.

This paper is general in nature and not intended as tax or legal advice. Because each employer is unique, an employer should consider its individual circumstances when evaluating a defined benefit plan administrative solution and should consult their retirement plan and/or legal advisor.

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