



STATE OF CONNECTICUT

# RETIREMENT SECURITY BOARD

CO-CHAIRS: STATE COMPTROLLER KEVIN LEMBO & STATE TREASURER DENISE L. NAPPIER

## Staff Report to CRSB

### Re: General Fiduciary Responsibilities

### April 1, 2015 CRSB Meeting

This memo provides only general guidance on fiduciary responsibilities and is not to be construed as legal advice.

#### Responsibilities

These responsibilities include:

- Acting solely in the interest of plan participants and their beneficiaries and with the exclusive purpose of providing benefits to them;
- Carrying out their duties prudently;
- Following the plan documents (unless inconsistent with ERISA);
- Diversifying plan investments; and
- Paying only reasonable plan expenses.

The duty to act prudently is one of a fiduciary's central responsibilities under ERISA. It requires expertise in a variety of areas, such as investments. Lacking that expertise, a fiduciary will want to hire someone with that professional knowledge to carry out the investment and other functions. Prudence focuses on the process for making fiduciary decisions. Therefore, it is wise to document decisions and the basis for those decisions.

Following the terms of the plan document is also an important responsibility. The document serves as the foundation for plan operations. Fiduciaries will want to be familiar with their plan document, especially when it is drawn up by a third-party service provider, and periodically review the document to make sure it remains current.

Diversification – another key fiduciary duty – helps to minimize the risk of large investment losses to the plan. Fiduciaries should consider each plan investment as part of the plan's entire portfolio. Once again, fiduciaries will want to document their evaluation and investment decisions.

#### Potential Liability

With these fiduciary responsibilities, there is also potential liability. Fiduciaries that do not follow the basic standards of conduct may be personally liable to restore any losses to the plan, or to restore any profits made through improper use of the plan's assets resulting from their actions.

**DRAFT DOCUMENT**



A fiduciary should be aware of others who serve as fiduciaries to the same plan, because all fiduciaries have potential liability for the actions of their co-fiduciaries. For example, if a fiduciary knowingly participates in another fiduciary's breach of responsibility, conceals the breach, or does not act to correct it, that fiduciary is liable as well.

#### Limitations on Liability

##### Documentation:

However, fiduciaries can limit their liability in certain situations. One way fiduciaries can demonstrate that they have carried out their responsibilities properly is by documenting the processes used to carry out their fiduciary responsibilities.

##### Participant Control:

There are other ways to reduce possible liability. Some plans, such as most 401(k) and profit sharing plans, can be set up to give participants control over the investments in their accounts and limit a fiduciary's liability for the investment decisions made by the participants. For participants to have control, they must be given the opportunity to choose from a broad range of investment alternatives. Under Labor Department regulations, there must be at least three different investment options so that employees can diversify investments within an investment category, such as through a mutual fund, and diversify among the investment alternatives offered. In addition, participants must be given sufficient information to make informed decisions about the options offered under the plan. Participants also must be allowed to give investment instructions at least once a quarter, and perhaps more often if the investment option is volatile.

Plans that automatically enroll employees can be set up to limit a fiduciary's liability for any plan losses that are a result of automatically investing participant contributions in certain default investments. There are four types of investment alternatives for default investments as described in Labor Department regulations and an initial notice and annual notice must be provided to participants. Also, participants must have the opportunity to direct their investments to a broad range of other options, and be provided materials on these options to help them do so.

However, while a fiduciary may have relief from liability for the specific investment allocations made by participants or automatic investments, the fiduciary retains the responsibility for selecting and monitoring the investment alternatives that are made available under the plan.

##### Service Provider:

A fiduciary can also hire a service provider or providers to handle fiduciary functions, setting up the agreement so that the person or entity then assumes liability for those functions selected. If a fiduciary appoints an investment manager that is a bank, insurance company, or registered investment adviser, the fiduciary is responsible for the selection of the manager, but is not liable for the individual investment decisions of that manager. However, a fiduciary is required to monitor the manager periodically to assure that it is handling the plan's investments prudently and in accordance with the appointment.



Fees are just one of several factors fiduciaries need to consider in deciding on service providers and plan investments. When the fees for services are paid out of plan assets, fiduciaries will want to understand the fees and expenses charged and the services provided. While the law does not specify a permissible level of fees, it does require that fees charged to a plan be "reasonable." After careful evaluation during the initial selection, the plan's fees and expenses should be monitored to determine whether they continue to be reasonable.

#### Bonding:

As an additional protection for plans, those who handle plan funds or other plan property generally must be covered by a fidelity bond. A fidelity bond is a type of insurance that protects the plan against loss resulting from fraudulent or dishonest acts of those covered by the bond.

#### Monitoring a Service Provider

An employer should establish and follow a formal review process at reasonable intervals to decide if it wants to continue using the current service providers or look for replacements. When monitoring service providers, actions to ensure they are performing the agreed-upon services include:

- Evaluating any notices received from the service provider about possible changes to their compensation and the other information they provided when hired (or when the contract or arrangement was renewed);
- Reviewing the service providers' performance;
- Reading any reports they provide;
- Checking actual fees charged;
- Asking about policies and practices (such as trading, investment turnover, and proxy voting); and
- Following up on participant complaints.

#### Reporting

##### Reporting to Participants and Beneficiaries:

The Summary Plan Description (SPD) -- the basic descriptive document -- is a plain language explanation of the plan and must be comprehensive enough to apprise participants of their rights and responsibilities under the plan. It also informs participants about the plan features and what to expect of the plan.

The Summary of Material Modification (SMM) appraises participants and beneficiaries of changes to the plan or to the information required to be in the SPD.

An Individual Benefit Statement (IBS) provides participants with information about their account balances and vested benefits. Plans that provide for participant-directed accounts must furnish statements on a quarterly basis. Individual account plans that do not provide for participant direction must furnish statements annually.

As noted above, for plans that allow participants to direct the investments in their accounts, plan and investment information, including information about fees and expenses, must be provided to



participants before they can first direct investments and periodically thereafter – primarily on an annual basis with information on the fees and expenses actually paid provided at least quarterly.

If a plan automatically enrolls employees, the Automatic Enrollment Notice details the plan's automatic enrollment process and participant's rights. The notice must specify the deferral percentage, the participant's right to change that percentage or not make automatic contributions, and the plan's default investment.

A Summary Annual Report (SAR) outlines in narrative form the financial information in the plan's Annual Report, the Form 5500 (see below), and is furnished annually to participants.

The Blackout Period Notice requires at least 30 days' (but not more than 60 days') advance notice before a 401(k) or profit sharing plan is closed to participant transactions. During blackout periods, participants (and beneficiaries) cannot direct investments, take loans, or request distributions.

#### Reporting To the Government:

Plan administrators generally are required to file a Form 5500 Annual Return/Report with the Federal Government. The Form 5500 reports information about the plan and its operation to the U.S. Department of Labor, the Internal Revenue Service (IRS), and the Pension Benefit Guaranty Corporation (PBGC). These disclosures are made available to participants and the public.

**The complete Department of Labor guide to general fiduciary responsibilities under ERISA can be found here: <http://www.dol.gov/ebsa/publications/fiduciaryresponsibility.html>**