



Fiduciary Considerations for Qualified Plans

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Who is a Fiduciary? – ERISA Definition

A person who:

- Has discretionary authority over plan assets
- Has discretionary authority over plan administration or
- Renders investment advice for a fee

Who is a Fiduciary? – Scope

- In General – limited to those assets over which the individual performs fiduciary functions
- Functional definition – cannot contractually limit scope of fiduciary duty

Who is a Fiduciary? – Settlor v. Administrator

- Settlor activities – not fiduciary
 - Establishment of plan
 - Termination of plan
 - Plan design decisions and amendments
- Administrator activities – fiduciary
 - Plan interpretation
 - Administering plan terms
- Co-fiduciary – can be liable for another fiduciary's breach if knowingly conceal, enable or fail to report/remedy the breach

Who is a Fiduciary? – Proposed definition

- DOL issued a proposed revised definition of fiduciary under ERISA in 2010
- Expanded the definition of who is a fiduciary by virtue of providing investment advice
- Proposed rule retracted by DOL September 2011
- Anticipated a re-proposal beginning 2012

Fiduciary Responsibilities

- Loyalty
- Prudence
- Diversification
- Consistency with plan

Fiduciary Responsibilities -- Loyalty

- Fiduciaries must discharge duties for exclusive purpose of
 - Providing benefits and
 - Defraying reasonable expenses of plan administration
- Avoid conflicts of interest
- Act in best interest of the plan
 - Actions may also benefit employer

Fiduciary Responsibilities -- Prudence

- Fiduciaries must act with
 - The same degree of care, skill, prudence and diligence
 - That a prudent person familiar with such matters
 - Would use in conducting an enterprise of like character and with like aims
- Prudent expert
 - Person who is not an expert must seek expert advice

Fiduciary Responsibility -- Follow The Plan

- ERISA requires fiduciaries to follow the documents and instruments governing the plan
- Plan documents and instruments must be consistent with ERISA
- Cannot blindly follow plan if it would be imprudent to do so

Fiduciary Responsibilities - Monitoring

- A fiduciary has a duty to monitor the choices it has made
- Hire an expert to perform monitoring function if the fiduciary does not have the appropriate expertise
- Process is important
- Make a record of questions, responses and actions taken

Prohibited Transactions

- Certain transactions between plans and parties in interest
- Parties in interest include
 - Plan fiduciaries
 - Plan service providers
 - Employers participating in the plan
 - Employees, officers and directors of participating employers

Fiduciary Responsibilities - Prohibited Transactions

- Direct or indirect
 - Sales, exchanges, leases
 - Loans or other extensions of credit
 - Furnishing of goods, services or facilities
 - Transfer or use of plan assets
 - Acquisition of employer securities or employer real property

Fiduciary Responsibilities - Prohibited Transactions

- Fiduciaries may not
 - Deal with plan assets for personal interest or accounts
 - Act in any capacity on behalf of a person adverse to the plan or participants (conflict of interest)
 - Receive any consideration for personal account from persons dealing with the plan (no kickbacks)

Fiduciary Responsibilities - Prohibited Transactions

- Limitations on investment in employer stock or employer real property
- Exceptions:
 - Up to 10% if stock or property is “qualified”
 - Up to 100% for ESOPS and other DC plans
 - 100% exception does not apply to 401(k) contributions if required to be invested in employer stock or property

Fiduciary Responsibilities - Penalties

- Fiduciaries are personally liable to make the plan whole for their breach
- Party in interest will owe excise tax in connection with prohibited transaction
 - Generally 15% of the amount involved for each year the violation continues during the taxable period
 - 100% of the amount involved if violation is not corrected
- Fiduciary acting as such is not subject to PT tax

Fiduciary Responsibilities – Participant Directed Investments

- Special relief for participant directed investments in defined contribution plan
- Plan must provide
 - Opportunity for exercise of investment control
 - Broad range of investment alternatives
 - At least 3 diversified alternatives

Fiduciary Responsibilities – Participant Directed Investments

- ERISA 404(c) does not protect:
 - Designation of investment alternatives
 - Transactions not in accordance with plan documents
 - Transactions that could result in losses in excess of account balance
 - Prohibited transactions
 - Losses due to actions of fiduciary carrying out instructions

Fee Disclosure – Fiduciary-level

- Effective date: July 1, 2012
- Effected plans: All ERISA-covered retirement plans except SEPs, Simple IRAs. Excludes IRAs.
- Content: Description of services and fees
- Timing: In advance of the contract
- Responsibility: Plan administrator

Fee Disclosure – Participant-level

- Effective date: August 30, 2012 for calendar year plans
- Effected plans: Individually directed defined contribution ERISA-covered plans, except IRA-based
- Timing: Initial, annual and quarterly disclosures
- Responsible party: Plan Administrator

Fee Disclosure – Participant-level (Content)

- Content:
 - Initial and annual disclosure:
 - General Information: designated investment alternatives and investment managers, brokerage windows, voting rights, investment direction rights
 - Expense Information: administrative fees and expenses charged against participant account
 - Investment-related Information: performance and benchmarking information, shareholder-type fees, restrictions on transfers, annual operating expense
 - Administrative Information: contact for more information
 - Quarterly disclosure: dollar amount charged against account during preceding quarter and description of services provided

Fee Disclosure – Participant-level (Format)

- Format

- Can be stand-alone or furnished as part of other documents
- Investment information reflected in chart form (model chart published by DOL) or other comparative format

Table 1—Variable Return Investments

Name/ Type of Option	Average Annual Total Return as of 12/31/XX				Benchmark			
	1yr.	5yr.	10yr.	Since Inception	1yr.	5yr.	10yr.	Since Inception
Equity Funds								
A Index Fund/ S&P 500 www. website address	26.5%	.34%	-1.03%	9.25%	26.46%	.42%	-.95%	9.30%
								S&P 500
B Fund/ Large Cap www. website address	27.6%	.99%	N/A	2.26%	27.80%	1.02%	N/A	2.77%
								US Prime Market 750 Index
C Fund/ Int'l Stock www. website address	36.73%	5.26%	2.29%	9.37%	40.40%	5.40%	2.40%	12.09%
								MSCI EAFE

Fee Disclosure – Participant-level (Enforcement)

■ Enforcement

- Disclosure is part of being a prudent fiduciary
- After a number of extensions, DOL will not give plan sponsors any more time, but when enforcing requirements, will take into account a good faith effort based on reasonable interpretation of the rules

Tussey v. ABB, Inc.

- ABB, Inc. sponsors two 401(k) plans, one for management employees and one for collectively bargained employees
- Fidelity provided record keeping services to the plans since 1995
 - Initially compensated on per participant fee, but later compensated from revenue sharing
- Class action in Federal district court in Missouri

Tussey v. ABB, Inc. – The Parties

- Plaintiffs were current and former employees of ABB, Inc.
- Defendants include:
 - Pension Review Committee
 - Named fiduciary
 - Responsible for selecting and monitoring plan investment options
 - Employee Benefits Committee
 - Plan administrator
 - Pension & Thrift Management Group of ABB, Inc.
 - Provided staff to Pension Review Committee
 - John W. Cutler, Jr.
 - Head of Pension & Thrift Management Group
 - Fidelity Management Trust Company
 - Fidelity Management & Research Company

Tussey v. ABB, Inc.

- Fiduciaries failed to monitor how much the plans paid for record keeping services
- Fiduciaries did not investigate market price of record keeping services
- Revenue sharing resulted in overpayment to Fidelity
- Fiduciaries argued expense ratios and progressivity, but were not successful

Tussey v. ABB, Inc.

- Investment policy statement expressly required
 - Rebates associated with plan investments to be used of offset cost of plan administrative services
 - Selection of lowest cost share class of mutual funds
 - Process for removing non-performing funds
- District Court found that the ABB fiduciaries:
 - Failed to follow plan documents
 - Selected higher cost funds to avoid per-participant record keeping fee
 - Failed to follow process for removing non-performing funds and relied on recommendation without investigation

Tussey v. ABB, Inc.

- Email from Fidelity suggested that revenue sharing from 401(k) plans paid for services to other ABB plans
- District Court found that ABB fiduciaries failed to follow up on that email and allowed 401(k) plans to subsidize ABB welfare and executive plans

Tussey v. ABB, Inc.

- Interest income from overnight investment of plan funds (float) was used for purposes other than for the exclusive benefit of the plans
- District Court found that float must be used exclusively for the plans

Tussey v. ABB, Inc.

- District Court awarded damages of nearly \$40 million
- Could have been higher if District Court had accepted plaintiffs' theory that damages should be based on defined benefit plan investment return

Tussey v. ABB, Inc. - Implications

- Periodic benchmarking of fees for plan services is essential
- Where multiple plans are involved, careful monitoring of revenue sharing is essential to avoid breach of exclusive benefit requirement
- Periodic review of plan documents to ensure that actions are consistent with policies and that policies are up to date

Questions?

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Sources

- ERISA Section 3(21)(A)
- ERISA Section 404 (a) and (c)
- ERISA Section 405(b)(3)(B)
- ERISA Sections 406 - 408
- DOL Regulation Section 2550.404a-5
- DOL Regulation Section 2550.408b-2
- Tussey v. ABB, Inc. 2012 WL 1113291 (W.D.Mo. March 31,2012)