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Avoiding Compliance Pitfalls: Getting Your Defined Contribution Plan In Shape

ERISA Compliance Overview

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Overview

- Definition
- Fiduciary Duties
- Fiduciary Liability
- Prohibited Transactions
- Fiduciary Compliance in Practice
- Plan Governance Considerations
- Management/Disposition of Plan Assets
- ERISA Reporting and Disclosure
- ERISA Claims and Appeals
- How ERISA Claims and Reporting Requirements Can Help You

Who is an ERISA Fiduciary?

- ERISA Section 3(21)(A): a person or entity who…
  - exercises discretionary authority regarding management or administration of the plan or disposition of plan assets; or
  - renders investment advice for a fee.

Who is an ERISA Fiduciary?

- Fiduciaries are determined through their **actions**.
- A plan must have at least one "named fiduciary" (ERISA Section 402(a)(1)), but there can be additional fiduciaries if there are parties that exercise such discretion, whether or not so designated in the plan document.

Who is an ERISA Fiduciary?

- An individual or entity can be a fiduciary with respect to some actions and not others.
- An employer (plan sponsor) acts a fiduciary when it administers and interprets the plan's provisions, but acts as a non-fiduciary ("settler") when it adopts, amends or terminates a plan.

Who is an ERISA Fiduciary?

- Examples:
  - Plan administrator (designated individual, or members of a committee)
  - Those who appoint committee members
  - Trustee
  - Investment adviser
  - Record keeper??

ERISA Fiduciary Duties

- **Duty of Loyalty** - Section 404(a)(1)(A)
  - Act solely in the interests of, and for the exclusive purpose of providing benefits for, participants and beneficiaries of the plan (and paying reasonable expenses of the plan).
    - Must set aside perspective as an individual participant AND as company management.
    - Importance of “wearing two hats” (fiduciary and settler).

ERISA Fiduciary Duties

- **Duty of Prudence** - Section 404(a)(1)(B)
  - Act with care, skill, prudence, and diligence of a prudent person acting in a like capacity and familiar with such matters.
    - Higher standard assumes experience, even if the fiduciary does not have such experience.
- **Duty of Diversification** – Section 404(a)(1)(C)
  - Diversify the investments of the plan to minimize the risk of large losses except where it is clearly not prudent to do so.

ERISA Fiduciary Duties

- **Duty of Compliance with Plan Documents** - Section 404(a)(1)(D)
  - Follow the terms of the plan documents unless doing so violates an overriding duty to act with prudence and loyalty.
  - Must either be familiar with the plan provisions or be advised regularly by someone who is.

ERISA Fiduciary Liability

- Each fiduciary is **personally liable** to the plan for any plan losses, and any benefits inuring to the fiduciary, which result from a breach.

ERISA Fiduciary Liability

- Co-fiduciary liability: a fiduciary can be held liable for a breach by another fiduciary if…
  - knowingly participates in the act or omission or knowingly acts to conceal;
  - its own breach enables the other fiduciary to commit the breach; or
  - knows of breach by other fiduciary and does not make reasonable efforts to remedy the breach.

Prohibited Transactions

- "Self-Dealing" Transactions - Section 406(b)
  - Must not act other than for the exclusive benefit of plan participants and beneficiaries.
  - Must not deal with plan assets for own account or in own interest.
  - Must not act in a transaction with the plan on behalf of any party whose interests are adverse to the interests of the plan, plan participants, or plan beneficiaries.

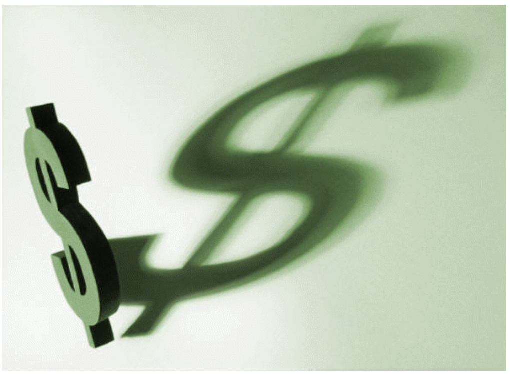
Prohibited Transactions

- "Party in Interest" Transactions - Section 406(a)
  - Must not cause plan to engage in transaction with a "party in interest" that is a direct or indirect:
    - Sale, exchange or lease of property
    - Loan of money or extension of credit
    - Furnishing of goods, services or facilities
    - Transfer of plan assets to, or use of plan assets by or for the benefit of, a party in interest.
  - "Party in Interest" includes:

Prohibited Transactions

- Exemptions: statutory exemptions and individual exemptions.
  - Essentially to allow normal business activities that do not otherwise violate the duties and responsibilities of fiduciaries.
  - Examples: payment of reasonable fees to service provider (e.g., trustee); plan loans to participants.

Prohibited Transactions



- **Consequences:**
  - Section 502(i) of ERISA and Section 4975(a) of the Code each provide for penalty taxes on a party in interest who engages in a prohibited transaction.
  - Reporting

ERISA Fiduciary Compliance in Practice

- Plan governance considerations
- Selected areas of plan sponsor fiduciary function:
  - Management/disposition of plan assets
    - Timely remittance of contributions
    - Selection and monitoring of investments
    - Selection and monitoring of service providers
  - ERISA reporting and disclosure
  - ERISA claim and appeal process

Plan Governance Considerations

- Who will be a named fiduciary?
- Designating committee members in plan document instead of via Board appointment
- Committee meetings and procedures
- Fiduciary training for committee members
- Third party service providers

Management/Disposition of Plan Assets– Timely Remittance of Contributions

- Amounts withheld from wages (e.g., 401(k) elective deferrals) become plan assets, and must be contributed to the trust:
  - on earliest date on which such amounts can reasonably be segregated from the employer's general assets;
  - but not later than the 15th business day of the month following the month in which they otherwise would have been paid to the participant.

Management/Disposition of Plan Assets– Timely Remittance of Contributions

- Per DOL, employer may not wait until the 15th business day of the following month to deposit deferrals if earlier segregation is possible. This is a significant area of non-compliance and audit.
- Contributions not timely deposited to the trust are considered an extension of credit from the plan to the employer. The employer is a party in interest, so delayed contribution is a prohibited transaction.
- Doll's VFCP? Safe harbor rule for small plans?

Management/Disposition of Plan Assets– Selection and Monitoring of Investments

- ERISA Section 404(c): participant-directed investment
- Fiduciary still must prudently select (and monitor) investment alternatives available to participants.
- Other 404(c) requirements:
- QDIA– qualified default investment alternative (gets 404(c) treatment)

Management/Disposition of Plan Assets–Selection & Monitoring of Service Providers

ERISA Reporting and Disclosure-
Summary Plan Descriptions

- Distribution Requirements…
  - To new participants within 90 days: SPD including all relevant SIMMs (summaries of material modifications).
  - To all participants, generally within 210 days after the end of the plan year in which amendment is adopted: SMM or restated SPD.
  - [Requirement to restate and distribute every 5yrs; every 10 if no changes; how terminated employees are handled]
  - Electronic delivery is generally allowed for both Spuds and SIMMs, [although there are some conditions which must be met].

ERISA Reporting and Disclosure-
Form 5500 (Annual Report)

- Plan administrators are generally required to file a Form 5500 which reports information about the plan to the Department of Labor, IRS, and PBGC.
- Contains information regarding the plan’s financial condition, funding, coverage, and any changes made to the plan during the preceding year.
- Plan audit required if …
- For plan years beginning in 2009, electronic filing will be mandatory.

ERISA Reporting and Disclosure-
Summary Annual Report

- Must distribute to each participant and beneficiary of the plan a summary annual report.
- Format prescribed by regulations.
- Must be furnished within nine (9) months after the close of the plan year. [confirm this– I think it is 2 months after 5500 deadline, w/ extension, so most are 12/15]

ERISA Claims and Appeals

- Must establish and maintain reasonable procedures governing the filing of benefit claims, notification of benefit determinations, and appeal of adverse benefit determinations.
- Description of procedures and applicable time frames must be in the SPD.
- Claim denial must be in writing and state specific reason for denial, must cite plan provision's) and include appeal instructions.

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ERISA Claims and Appeals

- Appeal Process
  - Every plan must afford a reasonable opportunity to any participant whose claim for benefits has been denied a full and fair review by the appropriate named fiduciary of the decision denying the claim.
  - Generally, a plan administrator must notify a claimant of the plan's benefit determination on review within a reasonable period of time, but not later than sixty (60) days after receipt of the claimant's request for review by the plan, unless special circumstances require an extension.

How the ERISA Claims and Reporting Requirements Can Help You

- Must exhaust administrative remedies before bringing a suit
- Allows qualified individuals to review potential lawsuits earlier in the process
- Ensures potential issues are dealt with in a timely fashion.