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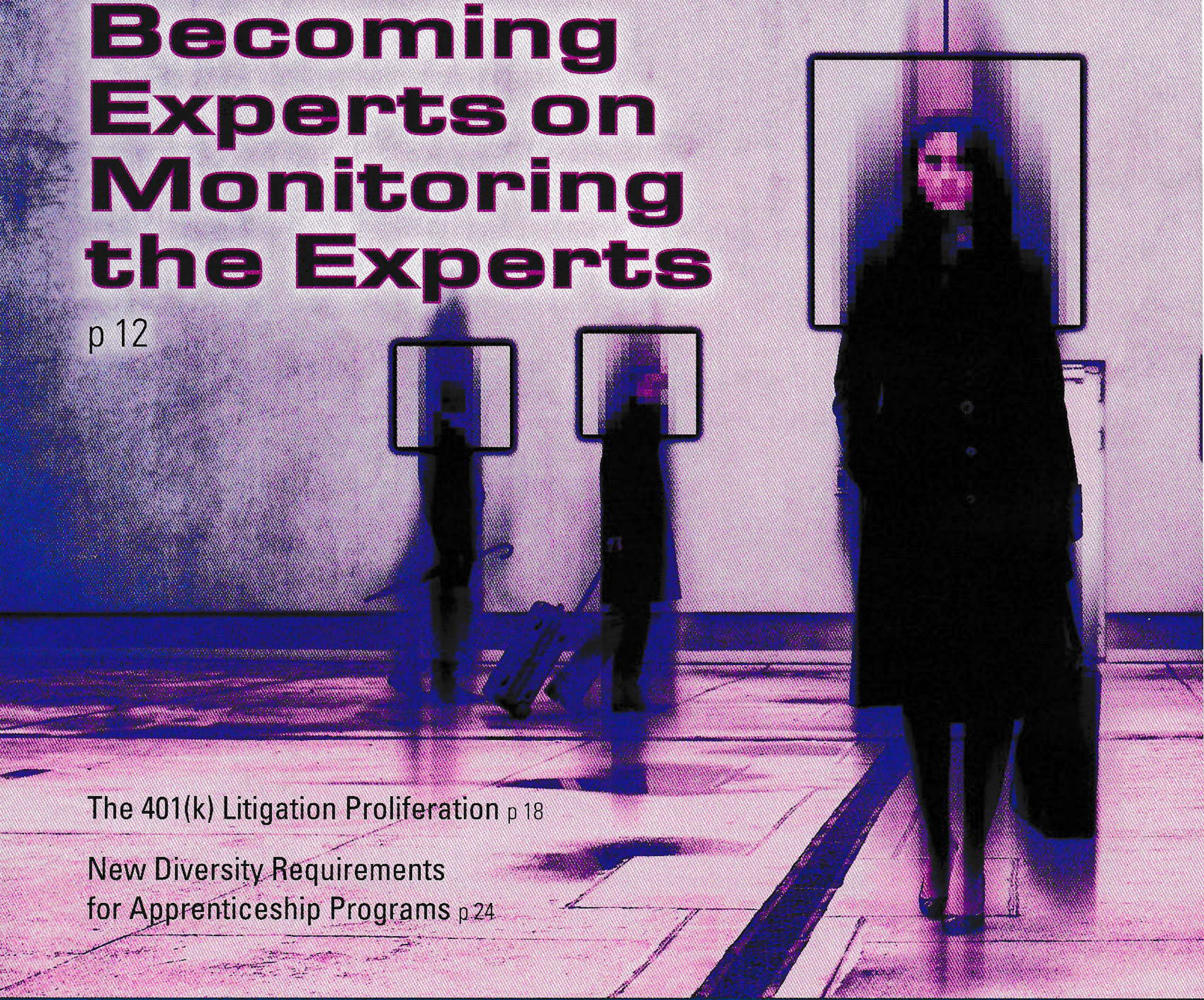

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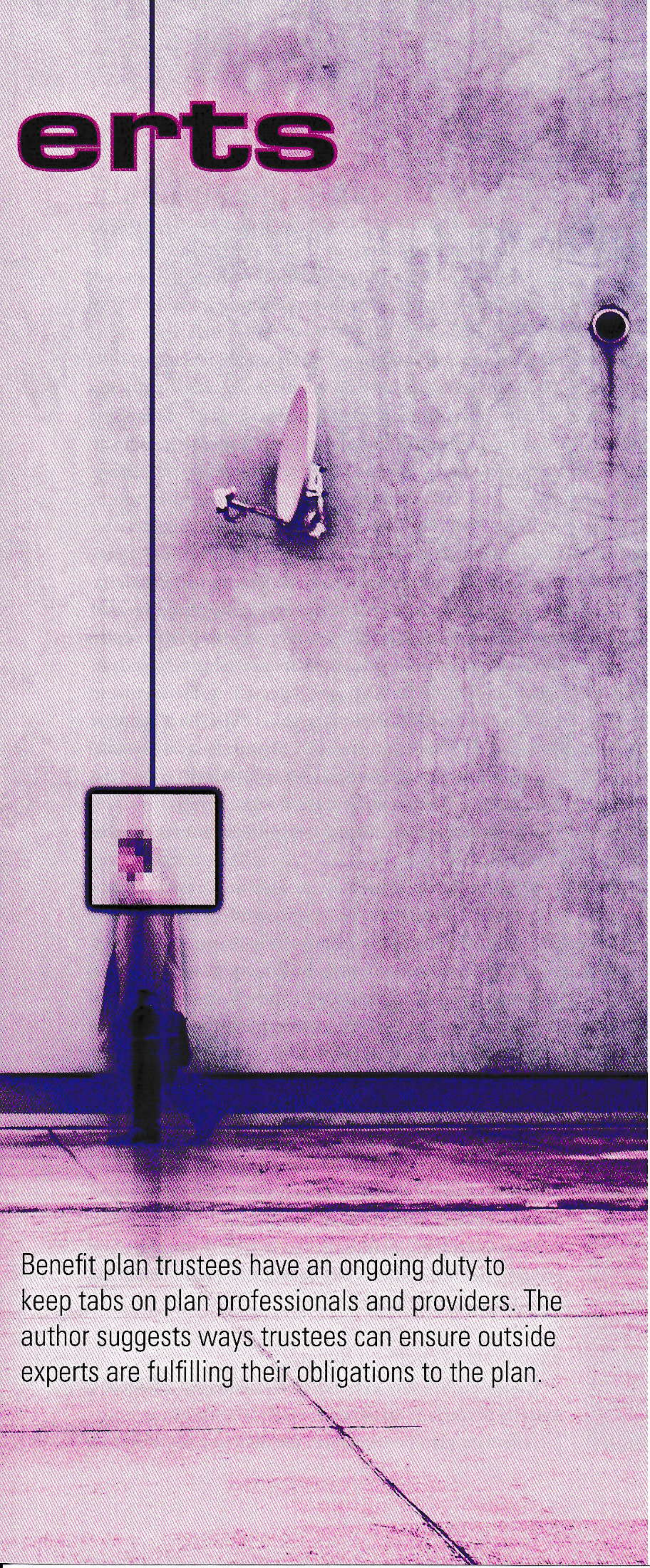

Benefit plan trustees have an ongoing duty to keep tabs on plan professionals and providers. The author suggests ways trustees can ensure outside experts are fulfilling their obligations to the plan.

Trustees have a duty not only to prudently select plan professionals, but also to monitor the quality of their work. This presents challenges for trustees who are tasked with ensuring experts are executing their duties and obligations with the requisite level of skill and knowledge.

No trustee can be skilled in all fields. Certainly, that is what the experts are for. But, trustees can become experts in monitoring the experts.

This article sets forth key principles and approaches for monitoring plan professionals and providers, a legal obligation requiring prudence and loyalty to participants.

Source of Legal Responsibility to Monitor Professionals

The act of selecting and monitoring plan providers is a fiduciary function. According to the Department of Labor (DOL), such activity is an exercise of discretion over the management and administration of plan assets. Thus, the person who selects a plan service provider is a fiduciary within the meaning of the Employee Retirement Income Security Act (ERISA) and subject to ERISA fiduciary standards.

A fiduciary has two all-encompassing duties:

1. The duty of loyalty (a.k.a. *exclusive benefit rule*). For providers, this means utilization and interaction for the exclusive benefit of participants.
2. The duty of competence (a.k.a. the *prudent man rule*). In this context, it means utilization and interaction with providers with the competence of one familiar with such matters.

Coupled together, these two duties equate to zealous advocacy executed with the skill of an expert with the sole aim to assist participants.

Because interaction with providers is so critical and subject to abuse if not properly monitored, there are conflict-of-interest rules and restrictions in dealing with service providers as set forth in the Prohibited Transactions Rules under ERISA §406. The most basic is that ERISA considers any payment to a service provider to be a prohibited transaction unless the service is necessary, the fee is reasonable and the arrangement can be terminated on a reasonable basis. Thus, such items should be the focus of the contractual relationship between the plan and the service provider.

Basics of a Contractual Relationship

As stated, payment of fees to a party in interest constitutes a prohibited transaction and breach of fiduciary duty unless the services are necessary, the fee is reasonable and there is a proper termination clause so as to not bind the trustees in a disadvantageous relationship. All three of these items should be the focus of the contract. More importantly, fee-based litigation is on the rise and should be a central focus. Other areas of focus include:

- **Boilerplate language.** This language may include disclaimers of obligations, limitations of liability in terms of fault and damages, restriction of judicial remedies (e.g., binding arbitration) and indemnifications.
- **Liability.** Trustees in charge of millions of dollars belonging to thousands of participants should have unfettered ability to sue anyone who causes damage to the plan. Providers may seek to restrict their own liability and have the reverse occur—have the trustees indemnify them for losses resulting from their own activity.
- **Insurance/bonding.** Trustees should make sure their providers will have the resources to satisfy any judgment or demand for payment arising out of their acts or omissions. Providers should provide insurance/bonding.

Reliance on Experts and Professionals

There is a widespread misconception that reliance on experts and plan professionals can insulate a trustee from liability. Some trust agreements have exculpatory language stating, for instance, that trustees who reasonably rely on plan professionals or act in good faith are not liable for any damages to the trust. This language is misleading, has no practical effect and runs counter to the core of ERISA obligations.

In reality, reliance on professional provider advice is only one factor to be considered in whether fiduciary duty has been fulfilled. The courts have ruled that:

- Fiduciaries are ultimately responsible for making careful choices.
- Independent expert advice does not provide a complete defense nor is it a "magic wand" to be waved over a transaction to ensure responsibilities are fulfilled.
- Determination of whether a fiduciary's reliance on an expert advisor is justified depends on many factors, including the expert's qualifications, thoroughness of the expert's investigation, whether the expert's opinion is supported by relevant material and whether the expert's methods and assumptions are appropriate.

Ultimately, the trustees are responsible for the integrity of the plan and, therefore, the obligation to make well-informed and careful decisions does not end with the selection of a plan professional.

Rather, a trustee's obligation to ensure that experts are performing their duties with the requisite level of skill and knowledge remains a constant.

Essentials of Ongoing Review

Under ERISA, any exercise of discretion by a fiduciary must be prudent. If that discretionary decision has an ongoing effect on plan performance, the fiduciary has a duty to

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From the Bookstore

Trustee Handbook: A Guide to Labor-Management Employee Benefit Plans, Seventh Edition
Claude L. Kordus. International Foundation. 2012.
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"monitor" (i.e., review) it. The duty to monitor exists separate and apart from the trustee's duty to exercise prudence in selecting plan professionals. The following are key areas of inquiry for ongoing review:

- **Bills/invoices.** A close review of the check register or invoices set forth at meeting agendas is an excellent source of information on plan activity—trustees will find who is billing the fund and for what services. It is often one of the first things DOL examines and questions trustees about.
- **Progress on assignments delegated to the provider.** Since the last report, has the provider made any progress and, if so, whether it corresponds with any billings/invoices.
- **Material items.** Make sure that, on any material items, providers supply a record of the activity—i.e., that they place the recommendations or activity in writing. Trustees can place these in the minutes or in separate correspondence. Generally, material items are substantive issues that require trustee decision making.
- **Employee or independent contractor.** Some funds choose to employ various providers and professionals. This makes the trustees vicariously liable in virtually all cases as opposed to situations for which the provider remained an independent contractor.
- **Size and history of firm.** The size of the firm is not as important as whether it can deliver services and address the fund's problems.
- **Fiduciary status of plan professionals and impact on trustee responsibility.** There are certain instances where professionals can be found to be fiduciaries (e.g., if they manage, control or make discretionary decisions regarding plan assets or step outside of their role and exert undue influence on the decision-making process). Some providers may assert that their fiduciary status relieves the trustee's own fiduciary responsibility. In most cases, it does not (except with the proper delegation of investments). A provider's status as a fiduciary simply means he or she is being held to the same standard of care as the trustee. Yet it does not protect the trustee against liability for the transaction.
- **Prohibited transactions.** As stated above, there is a class of transactions called *prohibited transactions* that Congress deemed so ripe for abuse that they must be avoided unless an exemption applies. Prohibited transactions are broad in scope and very specific. While it is beyond the scope of this article to discuss in detail, part of a trustee's ongoing review should ensure that:
  —All payments to service providers are for a necessary service, in a reasonable amount, and the contractual arrangement with the provider can be terminated on a reasonable basis.
  —The providers assisting trustees with the collection of contributions have a program in place to ensure trustees are making "reasonable, systematic, and diligent efforts" to collect contributions. Otherwise, it is considered an impermissible loan to a party in interest. Self-dealing includes dealing with plan assets in the fiduciary's own interest before his own account, acting in a transaction involving the plan on behalf of a party whose interests are adverse to the plan, and receiving consideration from any party dealing with the plan in a connection with a transaction involving plan assets. These categories include overt influence peddling, receipt of a discount from plan service providers on a fiduciary's own account and violation of prudent trustee reimbursement rules including unreasonable advances provided.

The above rules are detailed and complex, and many exceptions apply. Legal, accounting and administrators should be consulted to ensure the above rules are avoided and/or an exemption complied with.

takeaways

- Trustees have a fiduciary duty to properly select and monitor plan professionals.
- In assessing a contractual relationship with a service provider, trustees should ensure that the services are necessary, the fee is reasonable and there is a proper termination clause.
- Areas to watch out for in a contract with a service provider include disclaimers or obligations or limitations on liabilities.
- Independent expert advice does not provide a complete defense for trustees if a breach of fiduciary duty is alleged.
- Areas to look at in ongoing review of plan professionals include bills and invoices, prohibited transactions and the fiduciary status of plan professionals.
- Trustees should be careful about telling experts what to do. Instead, they should state the issue to their providers and ask for recommendations.

Motivation and Accountability

Understanding the trustee's role, plan professionals' roles and the duties and obligations of each is essential in navigating trustee interaction with plan professionals to ensure that trustee fiduciary obligations are being met while not assuming additional liability.

For example, trustees should use caution in telling experts what to do. Following instructions is the easiest thing for a provider to do and leaves the trustee unprotected if things go awry. Providers can say that they were just following instructions. Trustees should state the issue to their providers and have them provide their recommendations in writing—This tests their resources and imagination rather than manipulating them to a foregone conclusion.

Trustees should always ask simple, basic questions. Competing with experts in their own terminology or concepts likely will leave trustees confused, unsatisfied and maybe even reluctant to confess they didn't understand what the professionals said. Instead, trustees should ask for the experts' recommendations. For example, if they were trustees, what would they do in this situation? Is the contract exactly how they want it? Is the funding of the plan on a solid long-term basis? These simple questions shift the burden of a developing a solution to the professionals, which is why they were hired.

Aside from sundry or casual conversation, trustees should not formally rely on professionals who, either at the trustees' request or on their own, stray out of their own expertise. Sometimes trustees rely on an actuary for legal advice, a lawyer for actuarial or accounting advice or an administrator for all of the above. It is not prudent to rely on a professional outside of his or her expertise.

Professionals should not be lumped in a group. Sometimes trustees set up a so-called professional committee composed of perhaps an administrator, a legal accountant and others to provide recommendations. While these professionals certainly need to work together, they should provide independent advice in their independent disciplines.

Trustees should let the experts be the experts. Experts should not be coerced—implicitly or explicitly—to a foregone conclusion. Trustees should let them be independent, provide their own opinion and then engage with them in a rigorous analysis of their work product. Otherwise, they may just attempt to satisfy a trustee's professed objectives, which may or may not be prudent or in the best interest of participants.

Remedies Against Plan Professionals

If through careful monitoring of plan professionals it turns out that negligent performance inflicted harm to the plan, trustees have an affirmative duty to restore plan assets. While at liberty to let bygones be bygones with their own organizations' funds or personal finances, a fiduciary's personal predictions must not interfere with the zealous advocacy promised to participants. Thus, the trustees must take all corrective action necessary, including potential litigation, to make the plan whole.

Conclusion

Ultimately, the exercise of prudence is about having the right process for both the selection of plan professionals and the ongoing monitoring of the services they provide. The law does not dictate that a trustee must be an expert in all fields. Instead fiduciary duty dictates that trustees make careful, informed decisions when selecting experts to provide professional services to the plan, and prudence necessitates that trustees review the quality of the services such professionals provide. Of course, there is an art to dealing with this relationship. The key, as described above, is delegating full responsibility to the plan professionals to come up with innovative solutions that protect the plan and its trustees.

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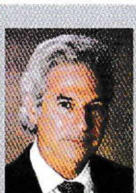

Michael J. Asher is a partner at Sullivan, Ward, Asher & Patton, P.C., a Southfield, Michigan law firm that specializes in labor, tax, investment and trial practice in addition to ERISA litigation. He has a B.A. degree from Kalamazoo College and a J.D. degree from the University of Detroit Mercy School of Law. Asher is a member of the International Foundation Professionals Committee.