PlanPILOT | Better Outcomes, Less Risk

EXECUTIVE SUMMARY

“What keeps you awake at night?” is a common question someone is asked usually when digging deeper into a person’s concerns and values. In today’s retirement plan world, the expanding role of the retirement plan fiduciary and the threat of lawsuits is likely to be near the top of responses to the question.

Over the last few years, there has been a proliferation of litigation against retirement plan sponsors and their fiduciaries, resulting in an increase in the number of settlements of lawsuits. According to a 2018 report from the law firm Seyfarth Shaw LLP, the Top 10 (i.e. largest) ERISA class action settlements have aggregated in the neighborhood of a billion dollars annually in each of the last few years, including $927 million in 2017.[1] Seyfarth notes an influx of 401(k) and 403(b) suits, with a particular concentration on higher education institutions. In particular, the cases focus on allegedly excessive fees for recordkeeping and plan administration, and investment related issues like share classes.

Further, one of the first higher profile 403(b) lawsuits was brought in 2016 against New York University (“NYU”) and its plan fiduciaries.[2] While some of the allegations have been dismissed in this and other suits, claims regarding excessive recordkeeping fees, conflicts of interest and failure to prudently monitor plan investment options continue. The complaint was recently amended to include the plan’s consultant for failure to provide prudent investment advice to the governing committee.

While there can be no assurance of being able to avoid litigation, there are steps a plan sponsor can take to minimize the likelihood and potential impact of lawsuits. These include:

1. Maintaining a clearly defined plan governance committee, process and documentation,
2. Regularly reviewing and, as appropriate, negotiating service providers’ services and fees, and
3. Having an effective process of investment monitoring, including fund fees and evaluating appropriateness of share classes.

Following is PlanPILOT’s guidance on how to effectively design and implement your retirement plan oversight functions and limit your exposure in these key areas.

1 14th Annual Workplace Class Action Litigation Report,” Seyfarth Shaw LLP, http://www.workplaceclassactionreport.com, January, 2018
2 Nevin E. Adams, JD, “New Grounds Emerge in NYU Excessive Fee Suit,” napa-net.org, http://www.napa-net.org/news/technical-competence/erisa/new-grounds-emerge-nyu-excessive-fee-suit, January 19, 2018

PART 1
GOVERNANCE CONSIDERATIONS

GOVERNANCE

One of the most critical items a retirement plan sponsor and its fiduciaries needs to implement is effective plan governance. This involves defining and training the retirement plan committee, running the committee meetings effectively, and maintaining thorough documentation of the structure and performance of the committee and its key decisions.

Defining & Training the Committee

The retirement plan committee serves as the backbone of any retirement plan governance structure. The committee is responsible for making many of the decisions regarding the plan and is often the named fiduciary of the plan as defined in ERISA. There is no single formula for creating the perfect committee, but there are common themes.

Size

Deciding how many committee members is appropriate is partly based on the organization's time, resources and demographics. A committee with more members provides the group with a greater amount of resources to perform plan-related duties, along with a more diverse spectrum of ideas and opinions from the different members. However, additional members may also create more complications with coordinating group meetings and communication conflicts.

A larger group may also cause delays in decision-making, which we refer to as "process losses." While more members may increase the productivity of the committee, they also increase the potential for process losses. At a certain point, actual productivity will begin to decrease with the inclusion of additional members.

We believe the optimal number of members is five. This helps to avoid situations in which a vote on a decision may lead to an even split (often causing significant process losses). If the plan sponsor elects to have an even number of committee members, we recommend the committee chair's vote serve as the tie breaker.

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Diversity

The next key decision is to select who will be on the committee. The members do not have to be experts in the retirement plan area, but they should have some level of familiarity with the plan and a working knowledge of investments.

Generally, members will include staff from the Human Resources and Finance departments, although adding representation from other areas of the organization (e.g. faculty) can prove beneficial in serving participants' best interests. Well-formed committees tend to have a more diverse group of members to offer more expansive skills, backgrounds and opinions.

Types of diversity to consider include:

- **Social diversity** — differences in age, gender, ethnicity, etc. We believe a level of diversity in this area is important in the context of the retirement plan committee to gain a better understanding of the needs and wants of different participant groups.
- **Informational diversity** — differences in skills, education and knowledge. This type of diversity tends to provide the most benefit to a committee or group. Having members with a variety of expertise and skill sets can provide a tremendous amount of value in decision-making.
- **Value diversity** — differences in values, commitments and priorities. While this can be somewhat beneficial, we seek to limit this type of diversity within the committee context. By aligning every committee member's values and commitments, the group can work much better with similar goals regarding the plan.

Leadership

Any committee can live or die by the strength of its leadership. A leader with the flexibility to adapt in various situations is generally found to be the most effective. The leader needs to be process (not outcome) oriented—it is the committee's job to arrive at the outcome and the leader's job to get them there. A strong leader helps to establish clear goals and to maintain the committee's focus—bringing the discussion back to the central point. The leader should promote comfortable sharing of disparate opinions and put measures in place to offset groupthink, while driving towards consensus decision-making.

Training

At the outset of forming a committee, and whenever a new member is added, it is important to provide formal fiduciary training to all retirement plan committee members. This training serves to ensure that all plan fiduciaries completely understand their roles and responsibilities and the key ERISA concepts that will drive all fiduciary decision-making. Fiduciary training should be supported by a formal fiduciary handbook that committee members are able to reference as needed in fulfilling their duties.

Going further, on-going fiduciary training at committee meetings is necessary to keep committee members apprised of regulatory changes, ERISA guidance and other matters relevant to the proper management of their plan. Effective committee training, education and support leads to deeper involvement by all committee members, and more decisive actions by committees as the members gain clarity and confidence relative to their roles and responsibilities and on their fiduciary obligation to act in participants' best interests.

Running the Committee

Communication is vital in order for the committee to operate effectively. The committee must encourage all members to actively participate in discussions to benefit from everyone else's skills and ideas. If members don't communicate their specialized skills and knowledge to other members, this will provide little to no benefit to the committee.

Committees typically meet at least every quarter, and members are expected to attend and be prepared for all meetings. Meetings may be held more frequently during times of transition or change, such as when the plan is changing plan service providers or investment managers.

Meeting agendas should be sent out beforehand so that members can be ready to discuss the important issues. A structured agenda with set discussion points and time limits will allow committee members to prepare and allocate sufficient time for the meeting. This reduces the risk of the meeting going over, which can potentially lead to significantly reduced focus on the topics at hand or members having to leave early due to other engagements.

Additionally, committees should set a limited number of discussion points for each meeting. Four to six is usually a good amount, but this will vary depending on the importance and time required for each of the topics. Attempting to cover too many topics may not be a very effective approach to conducting meetings. As meetings go on, members may begin to lose focus in the meeting. As a result, topics discussed later in the meeting may not receive as much thought and consideration.

Committees typically meet at least every quarter, and members are expected to attend and be prepared for all meetings.

Frequently, during the course of a meeting, tasks or follow-up items may be an outgrowth of the committee's discussion. It is important to log who is responsible for the specific task or follow-up and to track the completion of this task. This helps not only to track the assignment, but it also provides the venue for accountability at the next meeting.

Documentation

Proper documentation is vital for an organized and efficient committee. Documentation also helps to mitigate fiduciary risk by providing written evidence of plan compliance and due diligence.

All committees should designate one person, usually the committee secretary, to take meeting minutes at every committee meeting. This helps to document topics that were discussed as well as any decisions made. The minutes should document who attended the meeting and any decisions that were reached. They should also show the rationale for those decisions and demonstrate that a prudent process was followed.

Outside consultants or attorneys can provide or help develop committee documentation. Much of this documentation will help to limit the plan sponsor's fiduciary risk as they have a better understanding of the documentation that is necessary as well as an understanding of the language and content that is required or highly recommended. Some of the important documentation that can be provided or developed includes:

- Committee charter
- Committee member acceptance/resignation forms
- Fiduciary handbook
- Fiduciary acknowledgement forms
- Fiduciary compliance checklists
- Conflict of interest policy and disclosure statement
- Investment policy statement
- Quarterly investment reports
- Manager search report(s)
- Plan document review
- Plan design and structure review
- Fee policy statement
- Meeting minutes
- Record retention policy
- ERISA §404(c) compliance monitoring
- Service Provider Fee Disclosure ERISA §408(b)(2) review
- Participant Fee Disclosure ERISA §404(a)(5) review

PART 2
PLAN OVERSIGHT CONSIDERATIONS

OVERSIGHT

Beyond having a thoughtfully structured, executed and documented governance process, there are a couple of more substantive areas that have been the subject of lawsuits against plan sponsors and their fiduciaries – vendor service and fee benchmarking in addition to investment oversight and fees. Effectively managing these areas will help protect the plan sponsor and its fiduciaries, as well as provide an appropriate return on investment for the plan sponsor and the plan participants for the risks taken and fees paid.

Vendor Service & Fee Benchmarking

External vendors provide services to a retirement plan, particularly the recordkeeping and plan administration (e.g. enrollment, loans, distributions, discrimination testing and 5500 preparation). The committee needs to know and assess the services available along with the appropriate fees that the plan sponsor and the plan participants should be paying for those services. Additionally, it is necessary to be able to apply the appropriate degree of leverage necessary when service issues develop or service professionals are not meeting expectations.

It is beneficial to compare the services a plan utilizes and has available to it and what it pays for them to an extensive database of current vendor service and fees information. This will assist the plan sponsor in negotiating with the recordkeeper to incorporate the latest offerings available in the marketplace and the competitive fees for potential reductions.

If one has not been completed in a while, it is appropriate to conduct a request for proposal ("RFP") process to compare the existing provider(s) to alternative firms. A multi-phased approach may include some or all of the following:

Phase	Key Milestones
I	▪ Information gathering of all pertinent documents related to understanding current and historical services and fees ▪ Discuss any specific service issues with committee that should be explored with potential vendors ▪ Confirm timeline and milestones with committee
II	▪ Determine the appropriate providers that should receive the request for bid ▪ Draft bid request ▪ Distribute bid request to approximately five potential respondents ▪ Facilitate questions from bidders and provide responses to all bidders
III	▪ Prepare analysis of bidder responses ▪ Catalog all fees from responses ▪ Follow-up with bidders on any likely undisclosed fees
IV	▪ Summarize bidder responses and develop a written report ▪ Discuss report findings with committee ▪ Choose to retain / change provider
V	▪ Negotiate fees with vendor ▪ Develop performance and service standards ▪ Establish a fee policy statement

Please note in Phase V the establishment of a fee policy statement. The adoption of a fee policy statement helps meet the need identified in case law where the fiduciary role of prudence is largely measured by having and following a process. A fee policy statement provides the foundation for structuring and monitoring the plan's administrative fees.

Going further, contracts and service level agreements are necessary tools to document the expectations of the service providers. The resulting set of documents will be consistent with the overall governance philosophy and approach, and will place appropriate focus on the return on investment that the plan sponsor and the plan participants receive relative to the costs paid for those services.

Investment Oversight & Fees

A solid investment oversight process provides the framework for a retirement program to be more likely to obtain successful outcomes for its participants. All committee members need to fully understand the rationale, conviction, and process related to all investment advice and recommendations supporting its decisions centered on the investment options it makes available to plan participants.

Investment Policy Statement

The Investment Policy Statement ("IPS") documents the desired goals and objectives of the investment approach of the retirement plan and the principles to adhere when making investment-related decisions. The document will include the appropriate risk and return measures that are customized for each asset class, and will be the guidepost for the manager selection and monitoring process.

Given the IPS is part of the foundation of the governance structure, it is vital to ensure the investment policy is followed and is reviewed and updated on a periodic basis. Recent case law has highlighted that adopting an investment policy statement but not complying leads to an increased risk level and potential financial penalty to the plan sponsor. The review process should be documented to ensure there is solid evidence of the oversight on this critical document.

Manager Selection & Monitoring

The process for selecting and monitoring managers has quantitative and qualitative aspects that avoid relying too heavily on quantitative data itself that can be misleading. This approach relies heavily on sophisticated software for quantitative analysis balanced with the practicality of qualitative analysis conducted by research staff.

While absolute returns (net of fees) are often considered a main indicator of investment performance, more emphasis should be placed on the risk-adjusted performance of investments. Given the importance of protecting plan participant dollars, risk control is of significant importance and must be evaluated and factored into all investment decisions.

Special consideration needs to be given to target-date or lifecycle funds. These funds are usually the qualified default investment option and are typically attracting the greatest share of the investment of current contributions. Considerations include the mix of asset classes, different investment styles (active, passive and blends), the glidepath or changes in allocations over time, whether the glidepath is managed to or through the anticipated retirement date, and the possible layers of embedded fees.

Risk control is of significant importance and must be evaluated and factored into all investment decisions.

Committees should hold quarterly investment review meetings to discuss both quantitative and qualitative fund data presented in the performance reports. These reports typically include an executive summary, review of performance and risk relative to the IPS, and individual fund reports.

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The on-going monitoring includes documenting when an investment fund's metrics do not meet investment policy criteria, whether a fund should be placed on a watchlist, and the recommended action steps, follow-through and, if appropriate, timeline for implementing investment changes. Specific action steps would include conducting additional independent fund research and initiating calls or meetings with investment managers/product specialists to address questions and concerns.

Fees

Further investment oversight includes monitoring the fees paid on the investment options. Comparing the funds a plan utilizes and the fees charged within them to an extensive database of peers assists the committee with finding the low cost options available, including different share classes, the use of passively managed funds, and the potential revenue sharing with the recordkeeper versus other fund options available in the marketplace.

Participant Education

It is paramount to have a thoughtful participant education process in place. This includes materials and on-line tools written in easy to understand, plain English, and is often supplemented with group presentations and on-site education meetings for participants. The committee needs to ensure what is developed and delivered to different demographic groups, and contains the messages that will provide participants with the appropriate tools, resources and investment structure to make appropriate retirement choices. Providing the investment structure to best fit the participant demographics, the right funds within that structure and the right share classes of the desired funds are all integral parts of developing a solid foundation that assists plan participants in managing their retirement income needs.

PART 3
BENEFITS OF USING A CONSULTANT

Support

Given the increasingly challenging and complex regulatory and litigation environment for retirement plans, it can be very beneficial for a committee to have an external retirement plan consultant. Consultants serve as a valuable resource to the committee due to the breadth and depth of their specialized knowledge in the retirement plan industry. Although committee members are not expected to be experts on retirement plan matters, consultants are experts and serve as co-fiduciaries with the committee.

Consultants can provide many direct and indirect benefits to the committee including:

- **Supporting committees.** As they meet with many committees with different dynaics and goals, consultants know what works and how to effectively encourage members to participate and make decisions. They will also know how to help everyone on the committee fully understand the topics being discussed and be able to update the committee on any relevant regulations or plan updates.
- **Knowledge of the common trends regarding the retirement plans** of peers and what is available in the marketplace. This helps to bring more ideas to the table and ensures that your plan does not fall behind your peers in attracting and retaining quality employees. Furthermore, thoughtful plan design will help ensure your employees are more likely to be retirement ready at an appropriate age.

CONCLUSION

Good retirement plan governance is key to a successful plan. The key to good governance is a well-run retirement plan committee that oversees the plan, its vendors and investment options, and the fees paid. Over the last few years, there has been a proliferation of litigation against plan sponsors and their fiduciaries. While there can be no assurance of being able to avoid legal claims, a plan sponsor can minimize litigation risk by taking the following steps:

1. Maintaining a clearly articulated plan governance committee, process and documentation,
2. Reviewing service providers services and fee benchmarking, and
3. Having an effective process of investment monitoring, including fund fees.

An expert consultant can assist the plan sponsor and its fiduciaries in accomplishing this effectively.

If you would like more information or guidance on creating more effective retirement plan governance, please contact PlanPILOT at info@planpilot.com or (312) 973-4911.

Take the next step.

Call (312) 973-4911 for more information or visit us at www.planpilot.com

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