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Why Are There Fiduciaries?

Decisionmakers need to be held to the highest standard

Under the Employee Retirement Income Security Act (ERISA), plan sponsors serve as fiduciaries for their retirement plans. Most often, the responsibilities they incur in that role are delegated to a committee and the committee members become fiduciaries. That is a heavy responsibility. It's also an unnatural one.

Committee members must put the interests of the employees ahead of both their individual interests and corporate interests. In other words, there is a primary duty of loyalty that runs directly to the participants; other duties are secondary.

That raises an obvious question: Why does the law require that employers have "fiduciaries"?

Viewed correctly, the answer is also fairly obvious. Committee members make decisions that impact the participants even more than they impact the company. Specifically, committees make decisions that materially affect the quality of the participants' lives in retirement.

Think about it. When investments for a 401(k) or 403(b) plan are selected, who is in the room? Committee members, an adviser and the provider. When decisions are made about plan and investment expenses, who is in the room? Again, committee members, advisers and providers.

More importantly, who is *not* in the room? The participants. They don't have a say in the investments in the plan, the plan expenses, the investment expenses, the use of revenue sharing, and on and on. Yet, who is most directly affected by those decisions? The participants.

Why do we have fiduciaries? Whenever there is an arrangement where some people—e.g., committee members—make decisions that can materially affect other people and those other people don't have a say in the decisions, the decisionmakers should be held to a higher standard of care. That's the requirement for a fiduciary.

ERISA imposes the fiduciary standard and "prudent man rule"—including that duty of loyalty—as well as the prohibited transaction rules to regulate the decisionmakers' conduct.

Going back to "Who is in the room?," wouldn't it be best if everyone present were a fiduciary? Wouldn't it be best if the adviser and the provider were also fiduciaries? Wouldn't it be best if everyone in the room were required to put the participants first in making recommendations and decisions? Arguably, it would be. But ERISA's legal structure doesn't require that, and in some ways, the act imposes restrictions on such a requirement, particularly for providers.

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Many advisers are fiduciaries, but many are not. How can a plan committee tell the difference? It's fairly easy. If an adviser says in writing that he, or the firm, is a fiduciary, then the adviser is. If the adviser doesn't provide such a written statement, then he, or the firm, isn't (or at least the adviser doesn't think so). The moral of that story is, if you want to ensure your adviser puts the interests of the participants first, just as you are required to do, then get it in writing.

On the other hand, few providers act as fiduciaries. That is, to a large degree, because of the prohibited transaction rules. A provider may make additional money from your investments in its affiliated mutual funds and receive income from mutual funds. However, it is a prohibited transaction for a fiduciary provider to recommend additional compensation (e.g., revenue sharing) for those investments. In other words, it would be a conflict of interest that the law forbids.

But I digress. Why do we have fiduciaries? Pure and simple, it's because the participants are not at the table, and somebody needs to look out for their interests.

Fred Reish is chair of the Financial Services ERISA team at the law firm of Drinker Biddle & Reath LLP. A nationally recognized expert in employee benefits law, he has written four books and many articles on ERISA, IRS and DOL audits, and pension plan disputes. Follow Fred on Twitter at @FredReish, and visit his blog at fredreish.com.

