Four Essential Skills For Retirement Plan Fiduciaries

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Investment returns are an easy, tangible measurement of fiduciary success. Right? In actuality, the management of investments is only one of four key skills that retirement plan sponsor fiduciaries should master (or appropriately outsource) to meet their requirements under ERISA. The other three disciplines – governance, administration, and controls – all have equally weighted importance in the realm of fulfilling fiduciary duty. And the tactical implications of the investments discipline are surprisingly different than most executives' perception. In this article, we will address all four necessary fiduciary skills – including defining what they really mean for retirement plan sponsors, and divulging practical tips on how to succeed in each area.

The lifeblood of a retirement plan is sustained by its investment outcomes. It seems almost intuitive, then, that anyone serving in a management capacity for a retirement plan should have better-than-average skills in the field of **investments**, and specifically, know how to manage the investment decision-making process. While the high visibility of investments makes this skill set an obvious one for most retirement plan executives, awareness about the other three key disciplines of ERISA fiduciary duty is often lacking. Yet, the disciplines of **governance**, **administration**, and **controls** combine to form the "trip wire" for many of the legal problems encountered by the ERISA retirement plan sponsor community. This article will de-bunk the currents myths about fiduciary duty, delve into the four critical disciplines that plan sponsors need to know, and discuss best practice tips for excelling in each area as a retirement plan sponsor.

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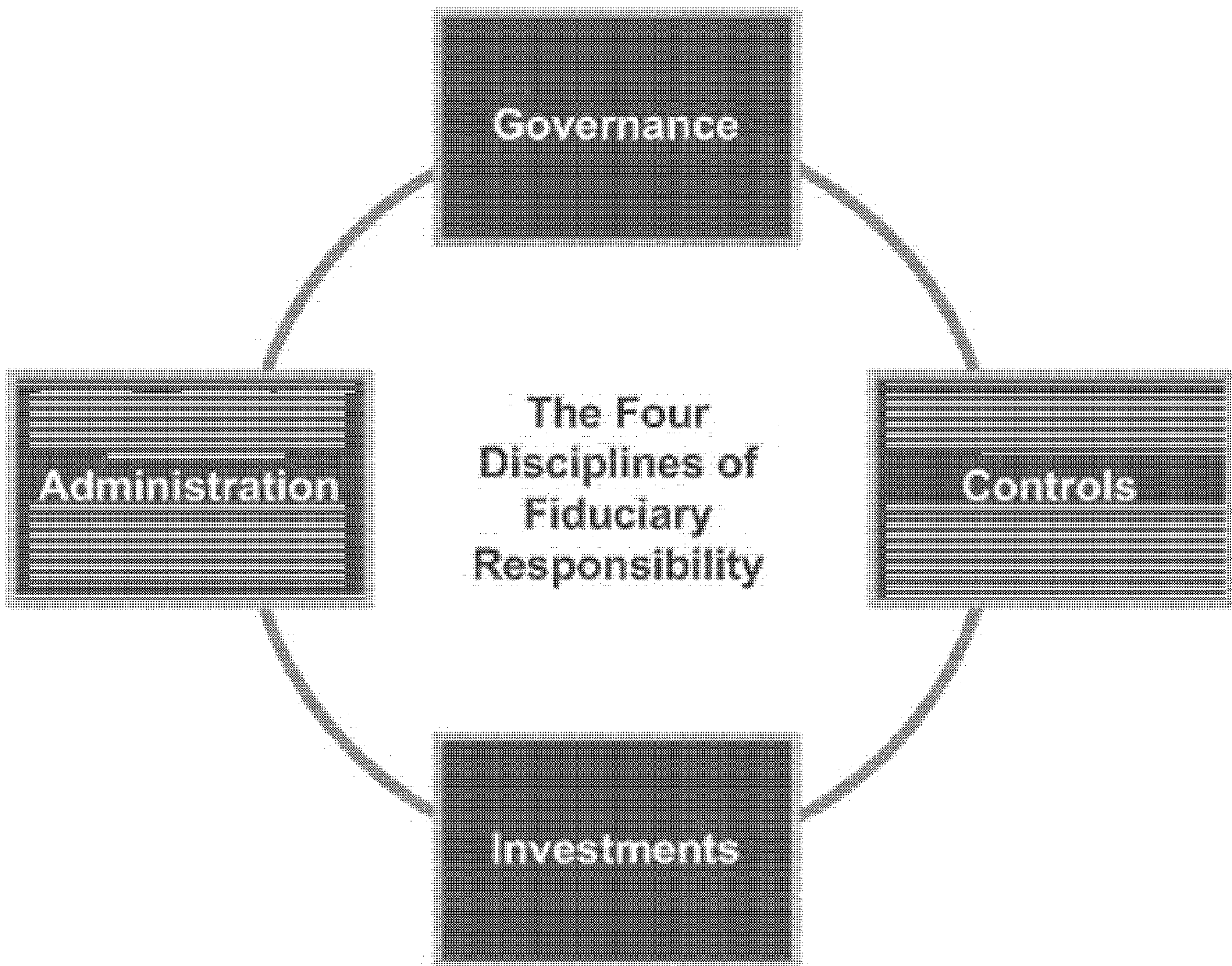

INVESTMENTS: JUDGING BY PRUDENCE, NOT MERELY INVESTMENT RETURNS

Let's begin with the (seemingly) most familiar skill to retirement plan sponsors: investments. Perhaps the singular biggest myth in fiduciary responsibility lies within this discipline. Due to the abundance of reports, presentations and marketing paraphernalia that many investment managers present to fiduciaries about investment selections and performance, fiduciaries often assume that their investment duty is about ensuring positive investment outcomes for their retirement plan participants. This, however, is NOT the definition of a fiduciary's duty under the investments discipline.

ERISA states that fiduciaries are to manage an investment decision-making process as a "prudent man" would do. Financial prudence is all about acting in trust of someone else's resources. Financial prudence implies that by executing ethical decisions on behalf of one's stakeholders, favorable financial returns should be a natural outgrowth. So, investment returns are actually a distant secondary measurement of a fiduciary's investment management skills — which are really measured by whether the investment *process* is being properly overseen.

Investments Discipline Objectives

The fiduciary objectives of the investments discipline, as published by global fiduciary standards organization Investment Fiduciary Leadership Council (IFLC), further expand on this notion. The fiduciary objectives for the investments discipline include:

1. Investment Managers' Fiduciary Support Processes Meet or Exceed Industry Best Practices
2. Investment Managers Are Selected Prudently
3. Investment Reports Are Reviewed Quarterly that Address Quantitative and Qualitative Issues

These objectives clarify the importance of overseeing a *prudent process* when it comes to selecting and supervising an investment manager, and having discussions that focus on the "right" issues (such as whether the investment advisor and/or vendor has conflicts of interest, or is selecting investments that pay the largest fees to his firm). An emphasis on objective #2, above, leads into the final piece of this discipline's discussion: how to leverage best practices to excel in the investments arena.

Investments Discipline Best Practices

Given the esoteric nature of the investment selection process, it is rare that a retirement plan fiduciary (typically, an executive or committee assigned to manage the company's retirement plan) has the background or knowledge to adequately act in an investment manager capacity for their company. Thus, a best practice for the investments discipline is to *select an experienced, independent investment manager* to manage the retirement plan's investments on behalf of the designated fiduciary. By focusing on evaluating the investment manager's process as opposed to specific fund selections, the investment role of the fiduciary is shifted to a role in which that fiduciary can excel. In addition, selecting an independent investment manager directly aligns with ERISA's preferred fiduciary model — having a true expert at the helm of each of the critical disciplines of fiduciary duty.

GOVERNANCE: LAYING THE FOUNDATION FOR SUCCESS

Governance is the definition of a retirement plan's chain of command and its scope of responsibilities. For fiduciary duty under ERISA, the governance discipline provides a structure for accountability. This skill set constitutes not only determining how a retirement plan management team will be organized and run, but also cognizance of whom is being selected for a leadership role, and why.

Governance includes naming the plan's internal fiduciaries, defining the scope of their responsibilities along with a training schedule, and setting policies for such topics as conflicts of interest, investments, and supply chain management. The governance discipline also embraces the creation and adoption of bylaws and guiding rules for this executive class.

A retirement plan's governance system should embody and support its vision, mission, core values, strategic direction, and employment principles. Key tenets of a properly developed governance system include the following: (1) The governance system should be efficient and effective, balancing the need for timely, informed decisions with the ability for meaningful participation by the primary fiduciaries in the decision-making processes, and (2) the governance system should provide for clear decision processes.

Governance Discipline Objectives

In line with these priorities of establishing a proper governance system, IFLC's stated objectives of this discipline include the following:

1. Authenticating Jurisdiction and Authority
2. Ensuring Fiduciary Competency
3. Developing and Maintaining Policies and Procedures

ERISA regards governance skills as a foundation for successfully carrying out the remainder of the disciplines. The quality of a retirement plan's governance approach determines the fiduciaries' ability and intent to fulfill ERISA's prudence requirements. It is no surprise, then, that a best practice of this discipline includes the education of this fiduciary management body.

Governance Discipline Best Practices

One of the most effective methods for ensuring success in this discipline is to *garner training for those members in the organization with a fiduciary role*. Many independent fiduciary firms will provide half- or full-day on-site training sessions that equip the fiduciary leadership team with the knowledge and confidence needed to implement and execute a plan for success. Some training also includes certification for fiduciary leaders — another recommended practice that can be repeated on an annual basis to ensure the company's fiduciary team stays abreast of key process adjustments and strategies for minimizing their risk.

ADMINISTRATION: FACILITATING PROPER PROCESS

The administration discipline includes the tools, technology and mechanisms used to carry out fiduciary responsibilities. With the U.S. Department of Labor's (DOL) heightened focus on this discipline in recent years, there is now more attention focused on how these responsibilities are being fulfilled. Prior to the DOL's decision to increase its audits of administration competency, many fiduciaries simply assumed that these responsibilities were being satisfied by their fiduciary vendors — and that, in turn, the fiduciaries' potential liabilities and risks were measurably lessened.

However, as scores of DOL audits now reveal, effective execution of ERISA's administration mandate requires up-to-date information systems and a quality management system monitored by capable personnel. This level of responsibility makes the administration of employees' retirement accounts an exceedingly demanding role — one that cannot be entrusted to an outside service provider that is not an acknowledged plan fiduciary.

A prudently constructed and monitored administration system should deliver comprehensive reporting on the performance of the retirement plan's portfolio, simplify government filings, offer Internet-enabled tools for the use of the primary fiduciaries and employees alike, and ensure the protection of the retirement plan's assets. These are just a few characteristics to consider when evaluating potential outsourced providers.

Administration Discipline Objectives

The objectives of the administration discipline, as outlined by IFLC, include:

1. The Practices of All Fiduciaries and Support Staff Are Evaluated Periodically for Compliance with Policies and Procedures
2. Service Providers Are Selected and Monitored Prudently
3. Administration Support Staff Members Are Trained and Supervised Properly
4. Reports to Donors and Regulators Are Accurate and Timely
5. Information Systems Support Is Designed to Meet All of the Needs of the Governing Body and Investment Fiduciaries

6. Transaction Processing Follows Defined Steps and Is Audited Annually

7. Physical Access to the Institution's Facilities, Information and Data Systems Is Restricted to Authorized Personnel

Administration Discipline Best Practices

Because the administration discipline entails direct information exchanges with plan participants, and due to heightened regulatory oversight, it is critical to ensure administration systems are working seamlessly. The best way to ensure that the most up-to-date resources are available to plan participants is to *outsource this fiduciary function to an accredited recordkeeping organization*. Again, as with the investments function, independence is key in selecting and partnering with a recordkeeper that will help serve the plan participants' best interests. A reputable recordkeeping organization can make a positive difference in the retirement plan experience for participating employees.

CONTROLS: ASSURING PARTICIPANTS AND PROTECTING FIDUCIARIES

The controls discipline includes the measurement of practices and progress against an established standard. ERISA encourages fiduciaries to measure not only what is done (performance), but also how it is accomplished (process). This reiterates the "prudent process" rule, as emphasized earlier under the investments discipline. Well-developed, consistently reviewed controls provide assurance to a retirement plan's participants and to the DOL that fiduciaries have implemented a stringent evaluation process related to the handling of their participants' accounts.

Controls, and the practices that are the subject of their oversight, are procedures performed routinely, some every day. An example is the act of completing a requisition form, obtaining approval, executing the approval, and storing a copy in the archives. Such an act is both a practice and a control — which is essential to tracking and recording key activities over time that relate to the overall fiduciary process. Properly performing controls functions can significantly reduce the risk of errors and omissions, which often expose fiduciaries to their greatest legal liabilities.

Controls Discipline Objectives

According to IFLC, the objectives of the controls discipline include:

1. Preempting Errors and Omissions

2. Detecting Errors and Omissions

3. Preventing Recurring Errors

4. Detecting and Evaluating Conflicts of Interest

5. Ensuring that Accounting and Financial Reporting Processes Are Effective

Of note is a recurring objective that appears in several of the fiduciary disciplines — "Detecting and Evaluating Conflicts of Interest." While errors and omissions in a fiduciary's internal processes can be the subject of a DOL investigation or enforcement action, it is often the actions of a fiduciary's *service provider* that cause a breach of fiduciary duty accusation. One of the most important controls practices is evaluating each service provider — in every discipline — to ensure 1) they are free of damaging conflicts of interest and 2) they do not charge inappropriately high fees for their respective services.

Controls Discipline Best Practices

An *annual audit of a retirement plan's management practices and service provider arrangements* is a foolproof way to ensure fiduciaries are risk-free and in compliance with ever-changing ERISA regulations. As fiduciary law moves further into the spotlight both for regulators and plan participants, it is important that fiduciaries take appropriate measures to document their efforts at maintaining the highest level of standards for the management of their plan. An annual audit helps to reinforce the message to both of these audiences that the company's leadership is a responsible steward of its stakeholders' valuable assets.

CONCLUSION: ROAD MAP TO FIDUCIARY EXCELLENCE

The issues faced by retirement plan fiduciaries are not static. Employees come and go, tax laws change, vendors' technical jargon evolves, regulatory focus shifts, reporting requirements grow more complex, and securities markets remain volatile. In order to keep pace, ERISA expects fiduciaries to achieve continuous improvement in their skills, methods, and results.

Across all four fiduciary disciplines, three activities universally can help fiduciaries to increase their acumen, sharpen their practices, and gain confidence in their retirement plan's strategic direction. These three steps include:

- *Awareness and Training*

  Policies and procedures are only as effective as the degree to which retirement plan executives and their vendors grasp their intent and execute them. Retirement plan fiduciaries who avail themselves of training regarding their role and responsibilities will take the first step in transforming the fiduciary assurance of their organizations.

- *Implementation*

  Engendering the confidence of participants and satisfying the DOL can be achieved by implementing a governance, risk, and controls ("GRC") system. Typically, this is a wholly outsourced program provided by an independent fiduciary advisor that seamlessly implements all four disciplines so as to protect the plan's fiduciaries and build confidence with plan participants.

- *Assessment*

  An inspection of a retirement plan's existing management system, measured against the four disciplines of fiduciary duty, is an excellent way to ensure alignment with industry best practices. The results of an assessment are confidential and used to maintain momentum for ongoing process improvements. As might be expected, the DOL supports the use of fiduciary assessments performed by qualified, unbiased, third-party experts. An annual assessment of a retirement plan's management system should be an integral part of its risk management program.

An awareness of the four essential fiduciary disciplines is the first step toward aligning with retirement plan management best practices as according to ERISA. But continuous improvement in the fiduciary realm does not have to mean large-scale change. By making small tweaks throughout the fiduciary journey, individuals and committees that manage plans of all sizes can take action to reduce defects, remove activities that do not add value to participants, and improve the balance between fees paid for retirement plan services and the quality of those services. Excelling in the fiduciary role is not a destination, but rather a continual path of growth, progress, and success.