Separating Fact from Fiction:

The Potential Risks and Rewards of Hiring a 3(16) Fiduciary

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Sentinel Benefits & FINANCIAL GROUP

Custom Solutions for Life and Wealth

Today's Speakers

John A. Carnevale, JD, AIF
President & CEO

- John Carnevale is a Founder and President of Sentinel Benefits & Financial Group.
- John oversees the management of four separate businesses and is primarily responsible for the company's vision and business development.
- During his 26 year career, he has acquired and integrated eleven businesses to grow Sentinel to one of the largest independent employee benefit firms in the United States.
- John graduated cum laude with a B.A. from Bowdoin College, Brunswick, ME in 1985. He earned his Juris Doctor degree from Suffolk University Law School in 1991. He earned his AIF in 2012.

Lisa L. Jones, Esq., CPC, QPA
Director of ERISA Consulting

- Lisa has over 20 years of experience working in the retirement plan area.
- Previously, Director of Compliance at CNA Trust and team leader of the Midwest ERISA plan specialists at Scudder Kemper Investments, all located in Chicago
- A member of the Illinois bar, Jones earned her law degree at Chicago Kent College of Law and a bachelor's degree in marketing from the University of Illinois at Chicago. She has attained the Qualified Pension Administrator (QPA) and Certified Pension Consultant (CPC) designations from the American Society of Pension Professionals & Actuaries.

Overview

- Retirement Plans have always been and continue to be complex
- There are many moving parts that require coordination to insure a successful result
- Success often depends on service providers, but responsibility for results lies squarely on the Plan Fiduciaries
- This webinar will discuss the various roles of plan fiduciaries, outsourcing these roles to fiduciaries and non-fiduciaries, and how to prudently select a fiduciary provider

Plan Administrator under ERISA 3(16)

- An ERISA 3(16) Fiduciary is responsible for **all decisions** related to a Plan, unless otherwise delegated to another fiduciary.
  - Must have discretionary authority or control over the management of plan assets or administration of the plan
- A plan must have at least one named fiduciary. ERISA Sec. 402(a).
  - A person
  - A committee
  - the corporation

Retirement Plan Management

Plan Sponsor or Other Named Fiduciaries

Plan Administrator

[ERISA 3(16)]

Big bucket of Fiduciary Responsibilities

Plan Management and Administration

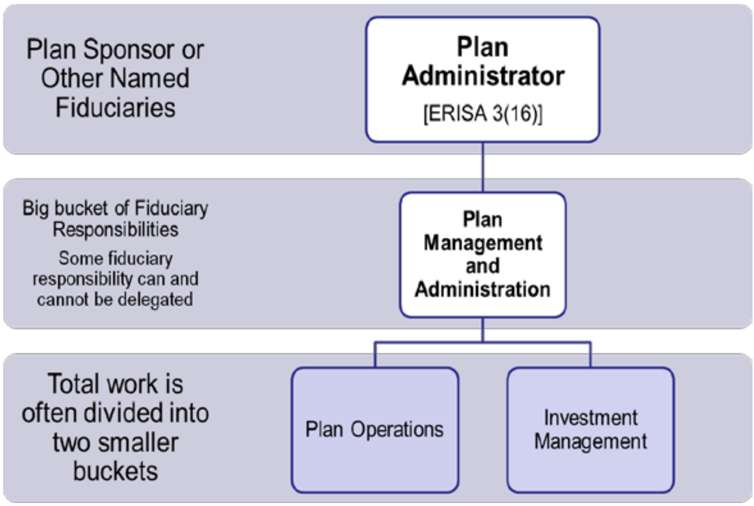
Total work is often divided into two smaller buckets

Plan Operations

Investment Management

Examples of duties of a 3(16) Plan Administrator

- Select, evaluate and monitor:
  - Trustee(s)
  - Administative Service Providers (fiduciary or non-fiduciary)
  - Investments Offered under the plan
  - Investment advisor to the plan, if any (RIA or broker)
- Decision to delegate plan administration and/or investment management responsibilities to <u>other fiduciaries</u>
- Evaluation of all plan fees



Fiduciary Basics

- Exclusive Benefit Rule
  - ERISA 404(a) requires a fiduciary to carry out his duties solely in the interest of plan participants and beneficiaries.
- Compliance with Plan Documents
  - ERISA Sec. 404(a)(1)(D) requires the fiduciary to carry out his duties in accordance with the documents and instruments that govern the plan.
- Diversification of investments
  - Diversification - ERISA Sec. 404(a)(1)(C) requires that investments be diversified to minimize risk of large losses unless, under certain circumstances, it is clearly prudent not to do so.
- Prudent Expert Standard
  - A fiduciary who is responsible for making plan or investment decisions is subject to a prudence standard that would apply to a person familiar with making such decisions.

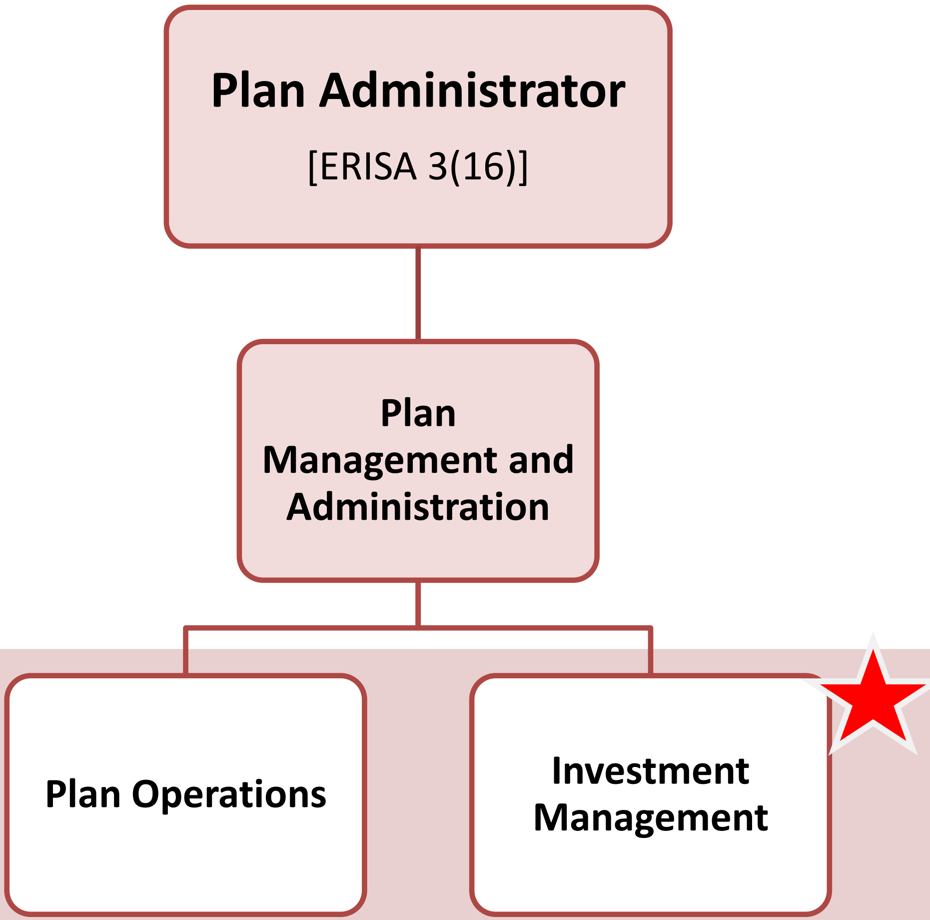
Consequences of Fiduciary Mismanagement

Personal Liability

ERISA Sec. 409 makes a fiduciary personally liable for any breach of responsibility that he directly commits, either by act or omission.

- Restoration of Losses
- Disgorgement of profits (return of profits gained as a result of a breach)
- Other relief determined equitable or remedial by the courts to compensate for a breach

Retirement Plan Management



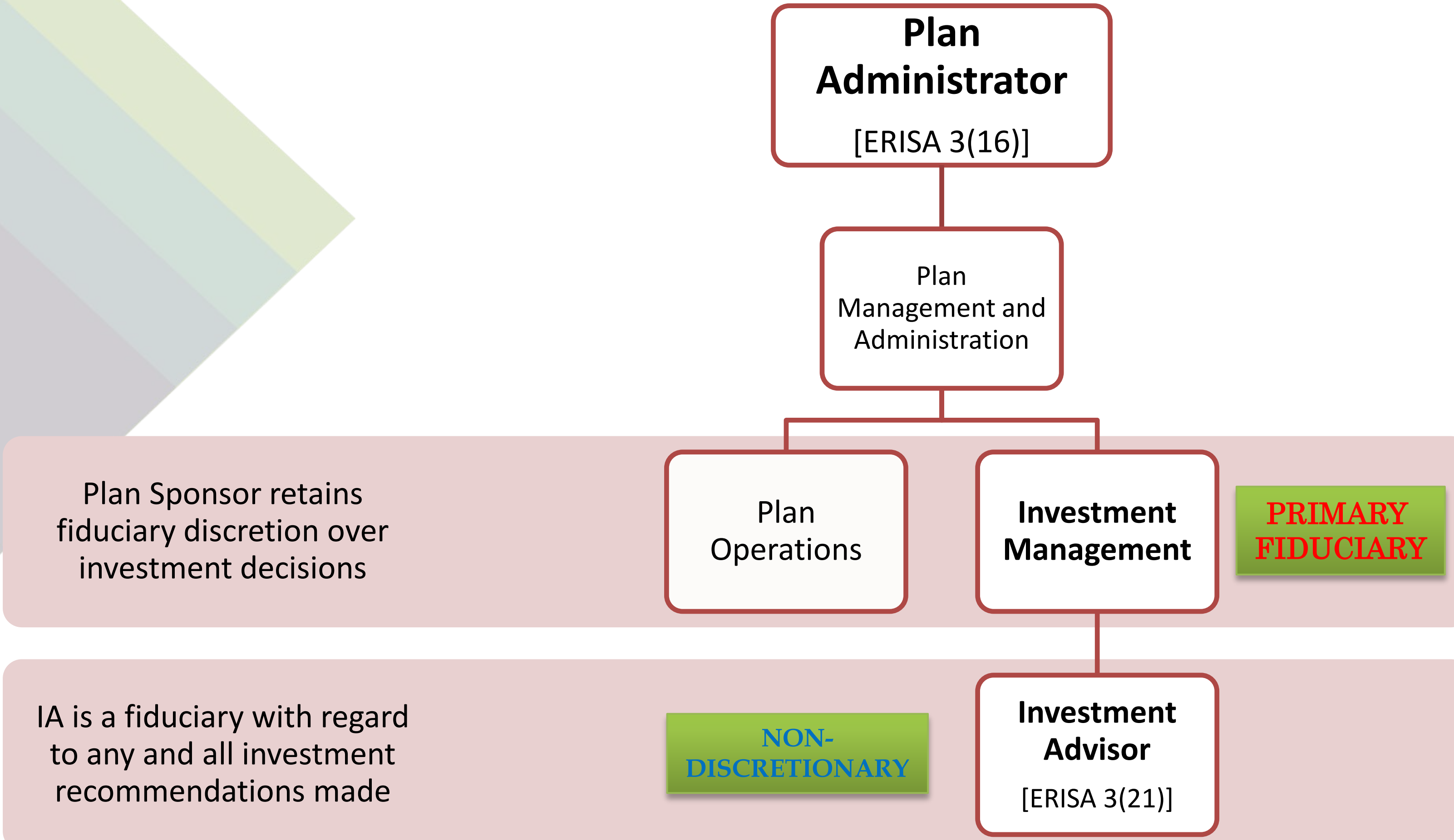
Engaging Investment Advisors and/or Managers – A popular trend

More Plans are Turning to Investment Advisors

- Delegating fiduciary responsibility to fee-only investment advisors has become a very common occurrence in the last few years.
- 82% of new plans sold in 2010 hired an advisor versus 69% in 2009
- The focus on fees in the last 12 months has accelerated Plan Sponsor interest in working with advisors
- To follow is a quick overview of how fiduciary delegation works from the investment perspective:

401(k) Exchange, May 2010.

Hiring an Investment Advisor [ERISA 3(21)]



Hiring an Investment Manager [ERISA 3(38)]

Plan Administrator

[ERISA 3(16)]

Plan Management and Administration

Plan Operations

Investment Management

Plan Sponsor delegates fiduciary responsibility for investment decisions, but must monitor IM

Investment Manager

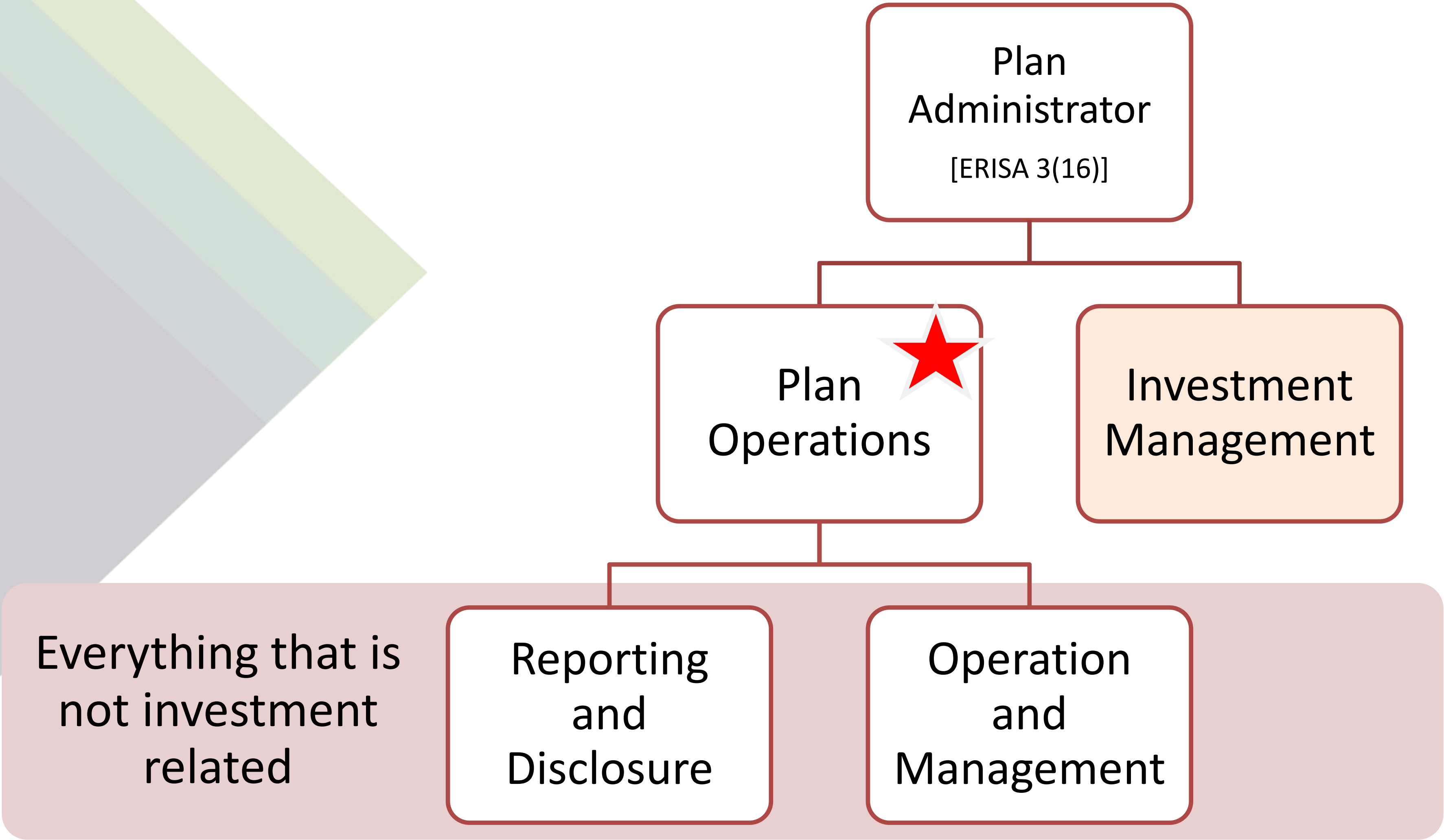
[ERISA 3(38)]

IM is the primary fiduciary with full discretion over investments

DISCRETIONARY

PRIMARY FIDUCIARY

Retirement Plan Management

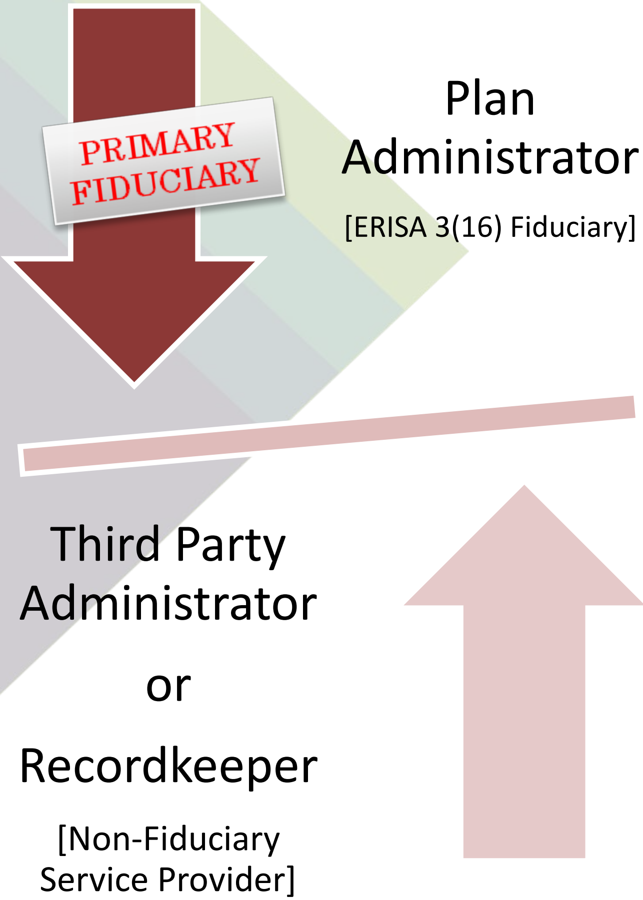


Examples of duties of a 3(16) Plan Administrator

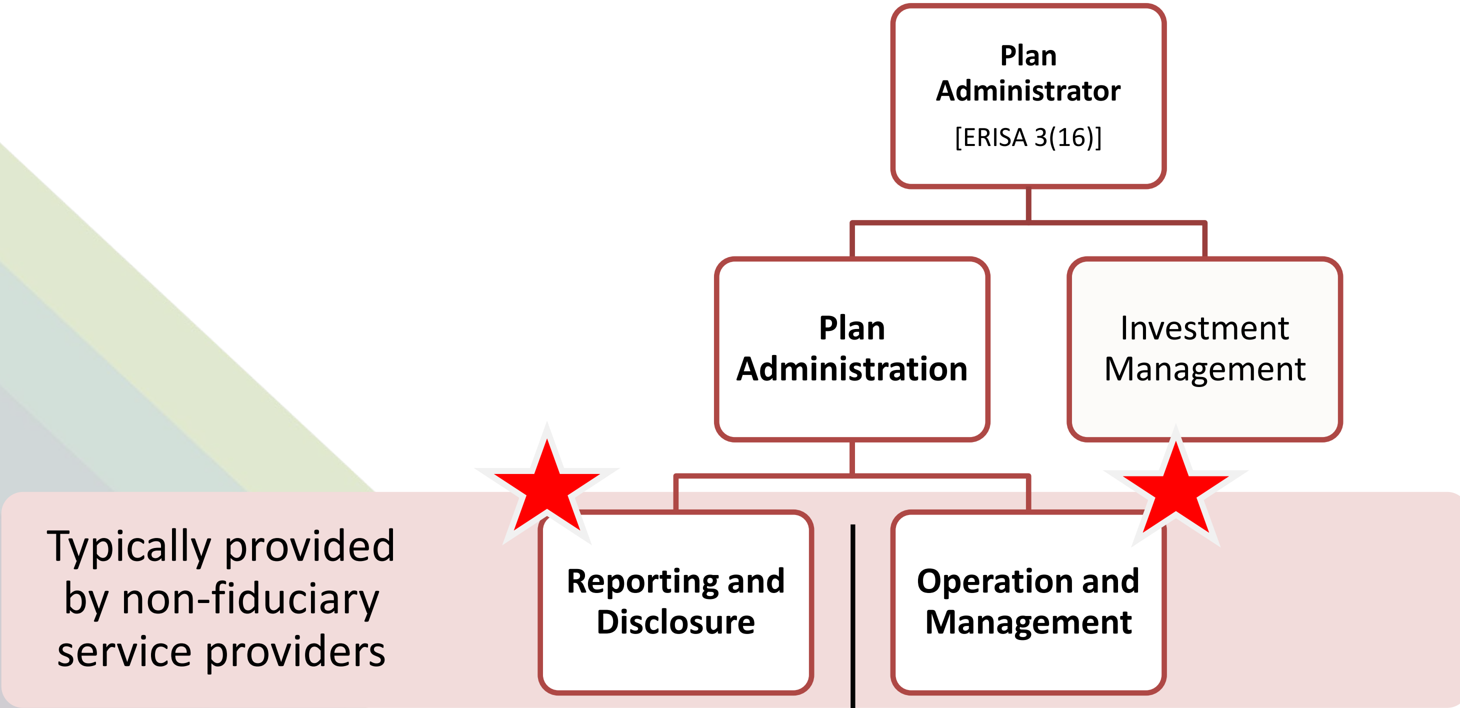
Plan Operations: (Not a complete list)

- Interpretation of the plan document
- Timely and accurate reporting and disclosure (e.g. Form 5500, distribution of SPD/SMM, participant fee disclosures, benefit statements, QDIA notices and other required participant disclosures)
- Distribution of benefits
- Administration of Loans, Hardship, and QDROs (develop procedures and process)
- Track Eligibility, Vesting and Beneficiary Forms
- Operate the Plan in accordance with the Plan Document

Typical Service Arrangements



- TPA’s and Directed Recordkeepers are **not fiduciaries**
- Service providers do not interpret the plan document and make discretionary decisions
- “Ministerial” services are non-fiduciary by nature



- Plan Documents
- Provide SPD/SMM
- Summary Annual Report
- Individual Benefit Statements
- 401k Safe Harbor Notices
- Automatic Contribution Arrangement Notice
- Qualified Investment Alternative Notice
- Participant Fee and Investment Disclosure
- 404(c) Disclosures
- Black-out Notices
- Provide Enrollment Information to new participants

- Administer distributions for terminated accounts
- Administer participant loans and hardships, including defaulted loans
- Track Eligibility
- Compliance Testing
- Adjudicating hardship withdrawals
- Approving QDRO’s
- Form 5500 Reporting

Raising the Stakes

- Plan Sponsors are seeking solutions to outsource more fiduciary responsibility for lots of reasons:
  - Managing a retirement plan is not a core competency or profit center
  - The work requires cross-functional cooperation within companies (HR, Payroll, Finance … who's responsible?)
  - Business turnover creates gaps and inconsistencies, which increase fiduciary risk
- **The next evolution to fiduciary outsourcing is the emergence of 3(16) Plan Administrator service providers**

Buyer Beware

Not all 3(16) service offerings are the same

- Some plan sponsors may mistakenly believe that a 3(16) Fiduciary will automatically assume all of the Plan sponsor's responsibilities
- 3(16) Fiduciary duties can be segregated by contract and many providers are accepting only portions of the total fiduciary responsibility
- Named Fiduciaries should read contracts very closely to assure they understand what they are buying and what they are NOT buying

Advantage of Hiring a 3(16) Fiduciary

- Plan Sponsor ceases to be responsible for the applicable reporting and disclosure obligations under ERISA

and / or

- operation and management of the Plan as a whole

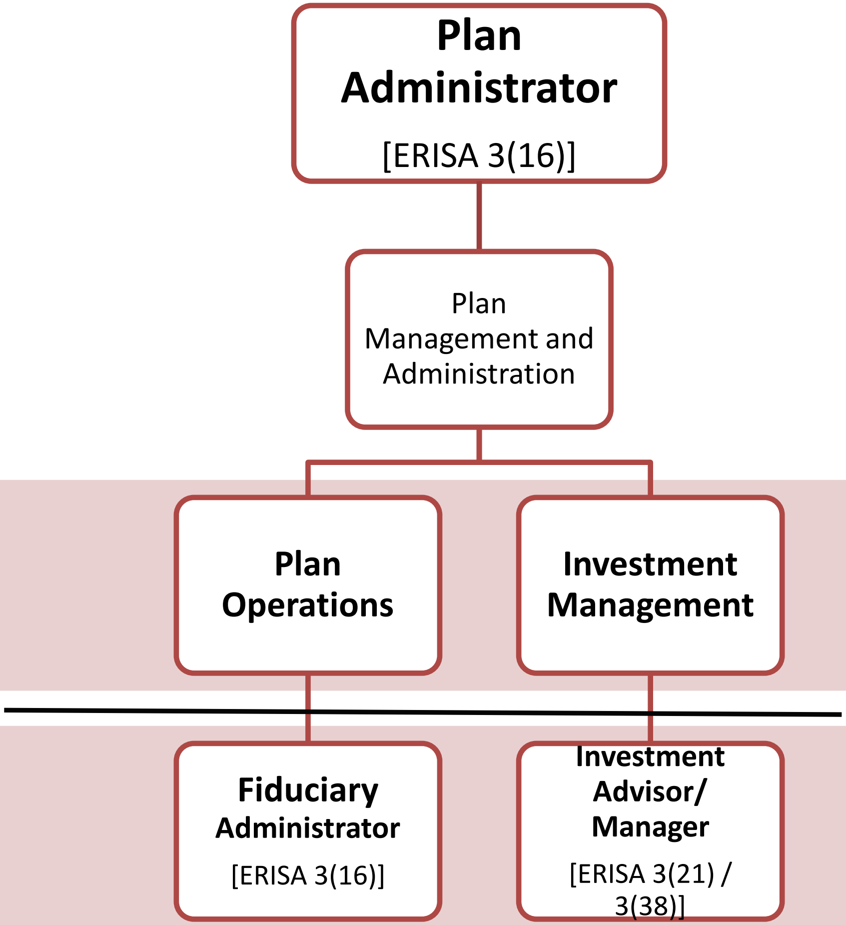
however

- **Plan Sponsor always retains fiduciary responsibility to select and monitor delegated fiduciaries.**

The Future Retirement Plan

Plan Sponsor monitors Fiduciary Administrator and Investment Advisor/Manager

Service Providers are Fiduciaries for all aspects of plan operations and investment management



How to Prudently Select a 3(16) Fiduciary

How to Prudently Select a 3(16) Fiduciary

- Establish and follow a procedure that satisfies the procedural requirements of ERISA.
- According to the DOL, engage in an objective process which is designed to elicit the information necessary to evaluate the following:
  1. The qualifications of the service provider
  2. The quality of services provided, and
  3. The reasonableness of the provider's fees in light of the services provided.

The Qualifications of the Service Provider

- ERISA Expertise
  - Confirm that provider has sufficient expertise in ERISA as well as the fiduciary standards that are imposed on Named Fiduciaries and Administrators under ERISA.
- Nature of Firm
  - Identify the size of the firm, the total amount of client assets under administration as well as whether the prospective firm is a trust company, RIA or non-regulated entity.
- Firm Experience
  - Request information concerning the firm's experience and track record in serving as a 3(16) Fiduciary, and the educational background and experience of the firms' employees and management team.

The Quality of Services Provided

- Level of Fiduciary Responsibility
  - Determine the extent to which the firm will accept any fiduciary responsibilities beyond those of a Third Party Administrator, and whether it will also be named as a Named Fiduciary for the Plan.
- Direct Services
  - The Plan sponsor should identify which direct services the 3(16) Fiduciary intends to render itself (i.e. TPA services, RIA services)
- Monitoring Services
  - Inquire how the firm intends to monitor and evaluate the services of other providers and their related compensation (i.e. formal evaluation, third part audit, fee benchmarking)

The Reasonableness of the Provider's Fees

- Fee Quotes for Comparable Services
  - Request bids or fee quotes from other comparable 3(16) Fiduciary firms to help determine the prevailing rate for similar services.
- Fee "Premium" for Accepting Fiduciary Role
  - If necessary, compare the firm's fee against the fees of comparable TPA firms offering non-fiduciary administrative services only, to determine the fee "premium" charged by the 3(16) Fiduciary firm for accepting fiduciary responsibilities.

Other Considerations

- Professional Liability (E&O) Coverage
  - Confirm that the firm maintains a sufficient level of professional liability coverage or errors and omissions insurance (i.e. $1 million) to ensure it will have sufficient assets to pay any potential claims made against it.
- Compensation for Investment Manager
  - If the firm intends to serve as Name Fiduciary and Investment Manager (in addition to Administrator), confirm that the firm will be unable to increase its compensation for services as Investment Manager in violation of ERISA's prohibited transaction rules.

QUESTIONS?

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