

# How can retirement plan sponsors minimize their investment liability by hiring the right ERISA 3(38) investment manager?

## Understanding 401(k) Investment Liability

In recent years, there has been an increase in lawsuits regarding employers who are allegedly breaching their fiduciary duties as trustees of their 401k plans. The particular concerns are whether they are prudently selecting and monitoring the 401k plan investment options offered, evaluating the associated fees that could impact investment returns, and providing timely reporting to the participants. The fiduciary standards apply to all Employee Retirement Income Security Act (ERISA) plans regardless of their size.

Most employers, while they may be good at running their businesses, may not be necessarily well versed in all their fiduciary duties as sponsors of these types of plans. No employer wants to find themselves in litigation over a 401(k) or be exposed for not performing their fiduciary duty.

Employers can mitigate their risks in this capacity, especially as it relates to selecting and monitoring the plan's investment lineup.



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One of the simplest and most effective ways for employers to minimize their liability from a poor investment lineup and to monitor oversight decisions of a 401(k) plan is to delegate the investment management to an “Investment Manager,” as defined under section 3(38) of ERISA.

Many employers are not aware of their fiduciary responsibilities to their 401(k) plans and plan participants. Knowing the various parties’ roles -who does what- and also who can take on some of the fiduciary responsibilities to reduce your risks, is critical.

### Roles and Responsibilities

There are four basic roles in administering and protecting the assets of a plan:

- **Custodian** - Safeguards assets of the plan and plan participants.
- **Record Keeper** - Fundamentally the bookkeeper for the retirement plan; maintains the records of who is in the plan and what investments they own. Also keeps track of and handles investment elections, contributions, and distributions.
- **Third Party Administrator** - Ensures the plan is administered in accordance with plan documents and that annual IRS compliance testing and filings are completed.
- **Investment Manager** - Creates and manages the plan’s investment lineup; selects, manages, and benchmarks the investments for the benefit of the participants.

Complaints against a plan sponsor could allege a breach of fiduciary duty for failure to prudently manage the investment options. This includes lack of focus, allowing excessive fees, and generally failing to carry out their oversight duties with the sufficient care, skill, and diligence of a prudent person (a high standard and requirement).

Under ERISA, a “Prudent Expert” standard is not that of a prudent layperson; rather it is that of a prudent investment professional. Not having a familiarity with investments is not an excuse. If a sponsor, acting as a fiduciary, cannot or is unsure of what to do in this area, they are expected to find and retain professional advisors to make recommendations.

## Finding the Right Type of Professional Advisor

This quest begins with knowing how much fiduciary responsibility you want to delegate. Plan fiduciaries generally have three choices when it comes to hiring third-party professional advisors, as each assumes different levels of fiduciary liability. The choices are: Consultants, Investment Advisors, and Investment Managers.

### Consultants

Consultants are hired to mitigate risk but take on no fiduciary liability for their investment recommendations. Sponsors have not delegated any responsibility or discretion and, as such, retain their full fiduciary responsibility.

### Investment Advisor

ERISA 3(21) Investment Advisors are hired as co-fiduciary liability. Under ERISA's fiduciary standards, their fiduciary responsibility is to deliver prudent investment advice. While an investment advisor retains liability for the investment advice they deliver, the plan sponsor retains discretion over making decisions related to the plan assets. And if the sponsor does not shift their fiduciary liability for selecting and monitoring their plan's investment options, they have effectively retained their fiduciary liability. It's almost like being in limbo.

### Investment Manager

ERISA 3(38) Investment Managers assume and retain sole fiduciary liability for investment selection and monitoring. When a plan sponsor chooses to hire an investment manager, it provides them with the greatest protection against claims related to poor investment selection and monitoring decisions. Choosing the right investment manager to select and monitor the plans investment options is the sponsor's largest liability.

## Choosing an ERISA 3(38) Investment Manager

Choosing an investment manager should not be taken lightly and should be done prudently. Understanding the manager's qualifications, experience, and other relevant factors begins with knowing what to ask.

Investment managers require a specialized understanding of retirement plan rules to meet their fiduciary obligations under ERISA. An investment manager's ERISA knowledge and experience are very important. Fiduciaries can be liable for imprudent investment selection.

Investment managers offer different services. Here are some basic offerings:

- Plan-level *and* participant level services.
- Plan-level *or* participant-level services.

#### Plan-level services often include:

- Investment Policy Statement (IPS) preparation.
- ERISA 404(c) assistance to participants and beneficiaries:
  - They can exercise control over assets in their individual accounts.
  - They can exercise independent control over their accounts.
  - They have access to a broad range of investment alternatives.
  - They have been provided with sufficient information to make informed decisions about the plan, investment choices and expenses.

#### Participant-level services often include:

- Model portfolios.
- Investment education.



## Modera Business Retirement Services

Modera Business Retirement Services provide additional non-discretionary services to help sponsors to meet their responsibilities and to minimize their risks:

### Administration support

Reviewing objectives and options available through the plan such as:

- Confirming sponsor's objectives.
- Reviewing available features of current or prospective platforms.
- Recommending features to achieve objectives.
- Reviewing and assisting with ERISA bonding amounts.
- Reviewing Fidelity insurance amounts.

### Participant education

- Group and individual one-on-one education format held in person or virtually, based on the needs of the plan sponsor.
- Review a broad array of investment options.

### Sponsor support

Assist sponsor with finding and evaluating other parties to the plan and fee benchmarking by:

- Evaluating the needs of the Plan/Plan participants.
- Reviewing utilization and satisfaction with services.

Delegating the investment management fiduciary responsibility is a choice. As well as you may have done with your own investments, do you want the responsibility and liability of making these decisions for your Plan's participants and their financial success?

When a sponsor hires an investment manager, they are delegating all the decision making for investment selection and monitoring. The investment manager's fund lineup cannot be changed by the influence of the sponsor without potentially foregoing the fiduciary protection they sought in the first place.

Sponsors who are successful in their business may find this trade off prudent, as this responsibility takes time and attention. Hiring an investment manager for investment selection and monitoring should give all participants, sponsors included, comfort.

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