Understanding the different types of fiduciaries

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Outline

• Introduction
• Fiduciaries as per the Investment Advisors Act of 1940 (1940 Act)
• ERISA 3(21) fiduciaries
• ERISA 3(38) fiduciaries
• Q&A
Introduction

• Current financial services environment very focused on fiduciary responsibility
• Increasing number of questions related to how one markets their fiduciary services and what is the associated liability
• When does marketing become too confusing or misleading?
1940 Act Fiduciaries

• Defines “investment adviser” as any firm or person that:
  • For compensation;
  • Is engaged in the business of;
  • Providing advice to others or issuing reports or analyses regarding securities.
• Includes money managers, investment consultants, and financial planners
• Excludes certain organizations and individuals (e.g. brokers, lawyers, and accountants, where services are incidental to conduct of their business)
1940 Act Fiduciaries

- Fiduciary duty imposed by operation of law as a result of relationship of trust established between advisor and client
- Clients include endowments, foundations, retail investors, retirement plans, and trusts
- 1940 Act and associated Rules specify acceptable conduct
Scott Pritchard, AIFA®

- Capital Directions, LLC
  - Atlanta-based RIA, with $800 million in AUM
  - www.capdir.com

- Advisors Access
  - Capital Directions’ turnkey 401(k) solution for RIAs
  - www.advisorsaccess.com
• Serve as a 3(21) fiduciary advisor in certain engagements.

• Serve as a 3(38) investment manager in other engagements, including Advisors Access, our 401(k) TAMP.
ERISA 3(21)

• Any plan sponsor that lacks the technical knowledge and experience to properly manage investments is required by ERISA to hire knowledgeable advisors.

• Historically, those advisors have been 3(21) fiduciaries.
Types of 3(21) fiduciaries

- Full-Scope: Effectively take the role of the plan sponsor in hiring and monitoring all service providers. Typically performed by an independent fiduciary.
- Limited-Scope: The predominant role played by advisors today and the focus of my comments.
Duties of a 3(21)

- Recommending investments to the plan sponsor.
- Monitoring those investments and suggesting replacements as appropriate.
- Providing participant education (can include one-on-one advice).
- Advising the plan sponsor in following a fiduciary process, including the Investment Policy Statement.
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Overview

- A 3(21) advisor provides counsel and guidance.
- A 3(21) advisor does not have discretion.
- Responsibility for investment decisions still rests with the plan sponsor.
W. Scott Simon, J.D., CFP®, AIFA®

- Prudent Investor Advisors, LLC (California-based SEC RIA Firm)
  - PIA is an ERISA § 3(38) Investment Manager operating as a discretionary investment fiduciary to retirement plans
  - www.prudentllc.com

- Prudent Retirement Services (a division of PIA)
  - PRS offers fiduciary turn-key outsourcing solutions to RIAs, B/Ds and TPAs nationwide (i.e., TAMP)
  - www.gotoPRS.com
W. Scott Simon, J.D., CFP®, AIFA®

- Columnist – Morningstar “Fiduciary Focus” since 2003 (fiduciary investment matters)
- Author – Index Mutual Funds: Profiting from an Investment Revolution
ERISA § 3(38) Investment Manager

- Appointed by Plan Sponsor to manage the investment process of the retirement plan (APPOINTMENT/DELEGATION)
- Only an RIA, a bank or an insurance company qualify to accept appointment (ACCEPTANCE)
  - Can a B/D be a § 3(38) Investment Manager?
- The Plan Sponsor–Investment Manager agreement must be in writing
- The Investment Manager must acknowledge its fiduciary status in writing
ERISA § 3(38) Investment Manager

- The Investment Manager becomes “solely” responsible for the selection, monitoring and replacement of plan investment options (DISCRETION)
- The Plan Sponsor and other plan fiduciaries are relieved of the responsibility for the Investment Manager’s decisions (FIDUCIARY RELIEF – ERISA § 405(d)(1))
- The Plan Sponsor retains a residual duty to prudently select the Investment Manager and make sure it is carrying out its appointed duties (OVERSIGHT)
ERISA § 3(38) Investment Manager

- The Investment Manager is not a consultant who “advises,” “recommends,” “assists” or “helps”
- The Investment Manager is a decision-maker with fiduciary discretionary authority who “decides”
- The Investment Manager is solely responsible for the day-to-day investment decisions (plan level)
- The Investment Manager does not provide fiduciary relief to a Plan Sponsor for poor investment decisions made by plan participants (404(c) provides this relief)
Fiduciary Outsourcing Model

Retirement Plan Sponsor

Plan Sponsor monitors IA, PRS, RK, TPA

Written agreement between Plan Sponsor and PRS appointing & delegating ERISA 3(38) fiduciary

Investment Advisory Agreement between Investment Advisor & Plan Sponsor

Client advisor and advocate, client relationship manager and quarterback

Memorandum of Understanding

Prudent Retirement Services (PRS)
ERISA 3(38) Investment Manager

Discretionary authority for selection, monitoring and if necessary replacement of plan investment options

Investment Advisor (IA)
ERISA 3(21) Fiduciary Advisor

Third Party Administrator (TPA)
- Compliance

Plan Record-keeper (RK)
- Custody
- Record-keeping
- Trading platform

Prudent Retirement Services
A Division of Prudent Investor Advisors, LLC
Questions?
Announcements—Thank you

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• Report attendance for one hour of CE for your AIF or AIFA designation on your next designation renewal form.
• Visit the fi360 Blog to continue the dialogue in the comments section: blog.fi360.com
• Email resources@fi360.com for any follow up questions
• The agenda for the 2010 fi360 Conference, May 5-7 in Orlando is now available: www.fi360.com/conference

• The 2010 AIF/AIFA Training calendar is now available—contact training@fi360.com to learn more about available options and special pricing for Webinar attendees!