

# REVERSE ENGINEERING 101: LITIGATION AVOIDANCE STRATEGIES

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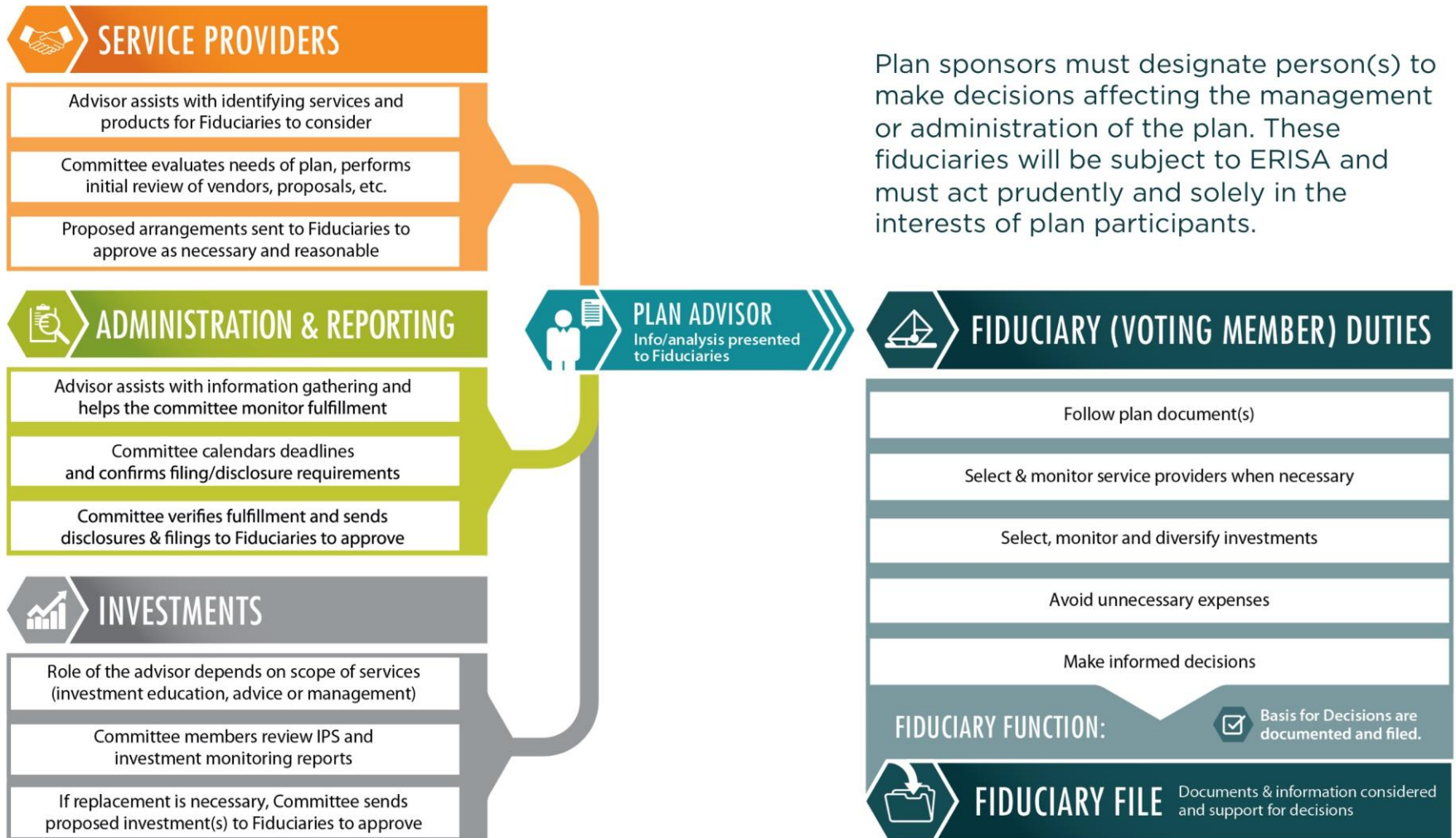


1. Legal Background;
2. Summary of Claims and Decisions in *Sacerdote et al. vs. New York University*;
3. Notable Quotes;
4. Best Practices for Best Interest™
5. Q&A

## Fiduciaries must act...

*"solely in the interest of the participants and beneficiaries,"  
and "for the exclusive purpose of providing benefits to  
participants and their beneficiaries; and defraying  
reasonable expenses of administering the plan."*

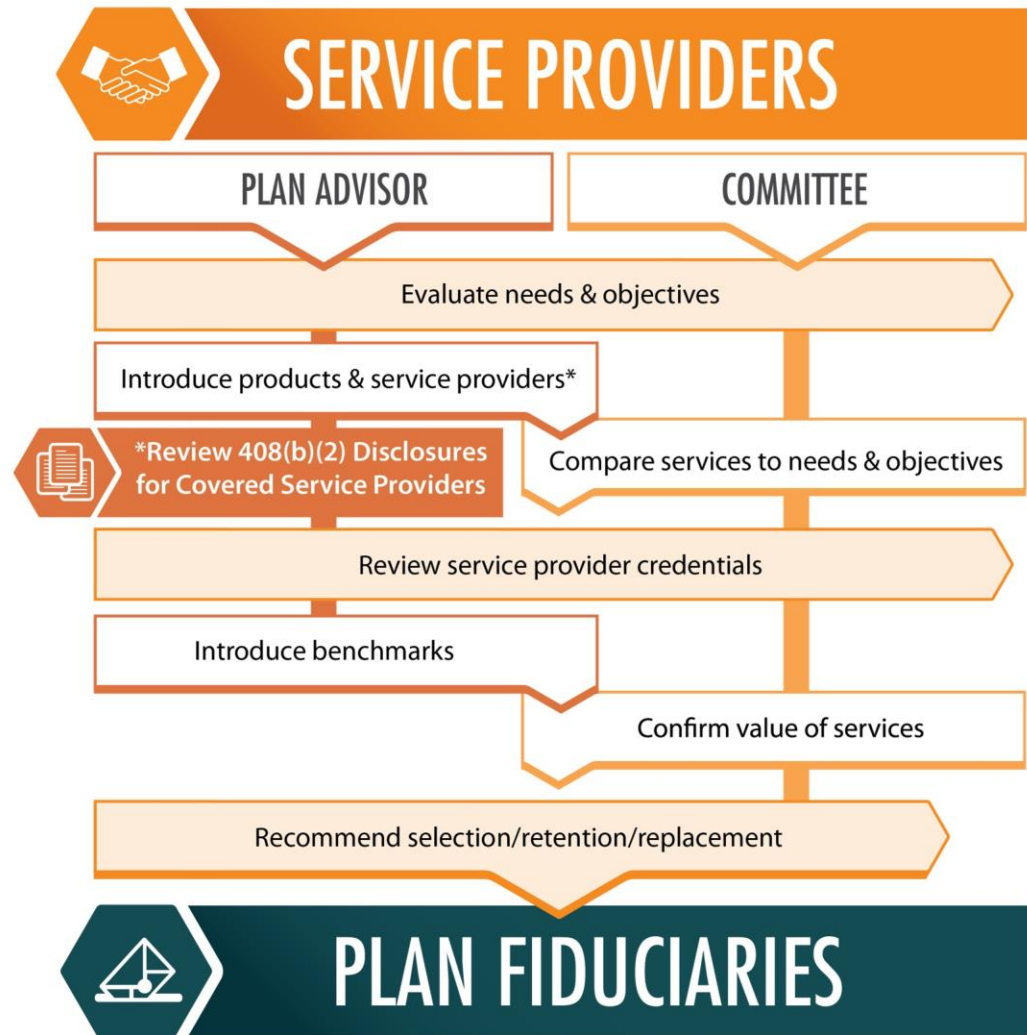
*See ERISA 404(a)(1)(A)*



Most plan fiduciaries require some degree of support in the service provider selection/monitoring process.

The flowchart on the right shows how an experienced retirement plan advisor can help.

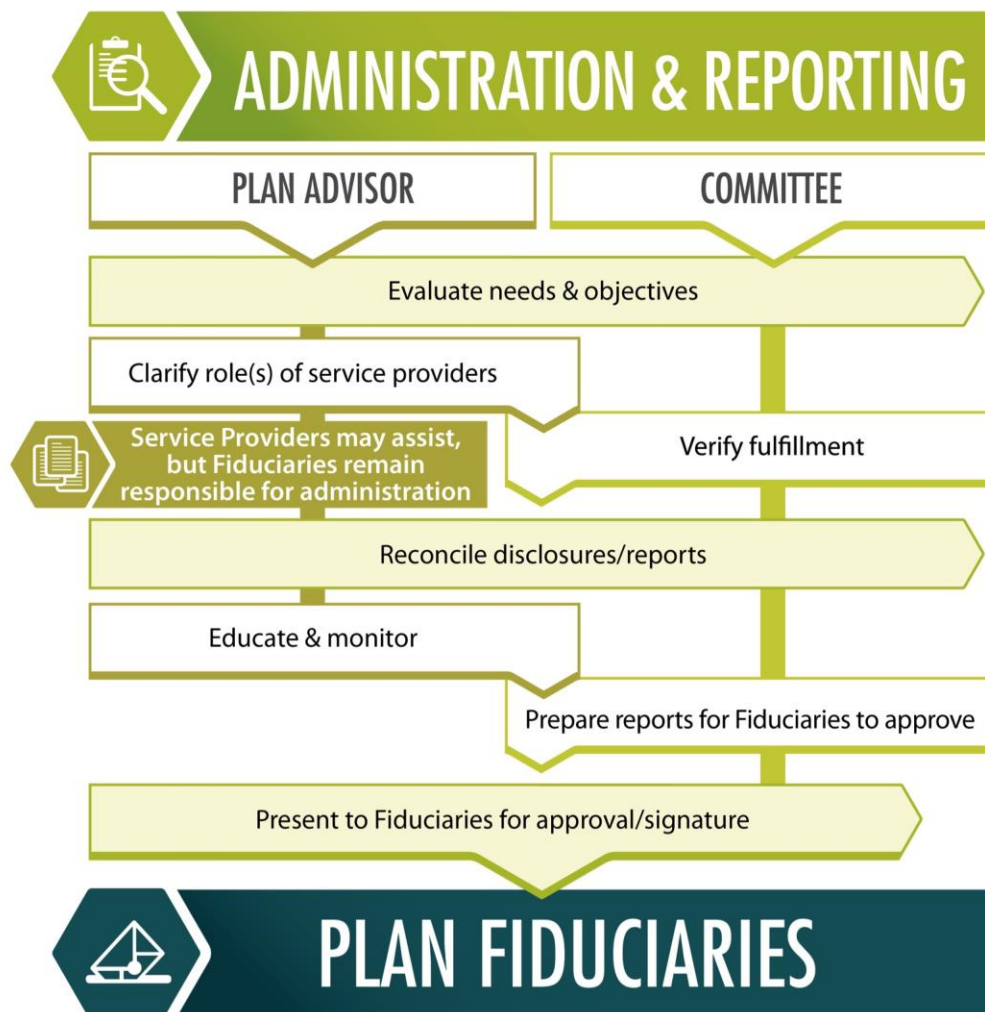
Note: Plan fiduciaries remain responsible for selecting, monitoring and replacing service providers.



Most plan fiduciaries require some degree of support in meeting the administration and reporting requirements.

The flowchart on the right shows how an experienced retirement plan advisor can help.

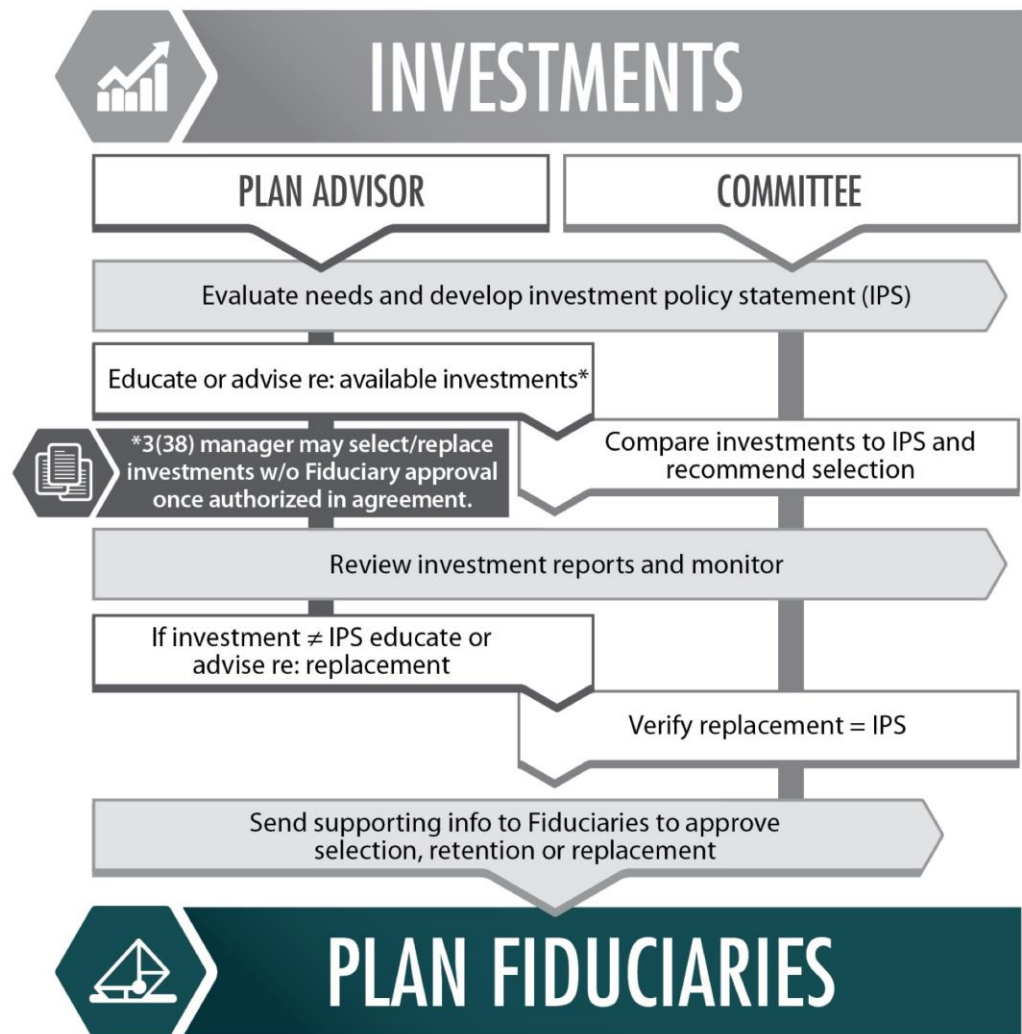
Note: Plan fiduciaries remain responsible for ensuring the plan is properly administered and all required notices/filings have been sent.



Most plan fiduciaries require some degree of support to prudently select and monitor investments.

The flowchart on the right shows how an experienced retirement plan advisor can help.

Note: Plan fiduciaries remain responsible for selecting, monitoring and replacing investments unless they have delegated to a 3(38) manager.





- Fiduciaries and committee members are educated and understand their roles and responsibilities;
- The plan is administered and operated in accordance with the Plan Document;
- Services provided to the plan are necessary;
- Expenses are properly paid from plan assets and CSP disclosures are current;
- CSPs are delivering services in accordance with the terms of their arrangements, and fees paid to CSPs continue to be reasonable in light of the value received;
- All notices and required disclosures and reports are timely and accurately delivered;
- Compliance documentation is retained and current;
- Investments are selected, monitored and replaced in accordance with the IPS; and
- Participants receive sufficient information from which to direct the investment of their individual accounts.





# To state a claim, plaintiff must allege...

- Facts that permit a plausible inference that the defendant "engag[ed] in transactions involving self-dealing or otherwise involve or create a conflict between the trustee's fiduciary duties and personal interests."
- "To state a claim for breach of fiduciary duty under ERISA, Plaintiffs must adequately allege that (1) Defendants were fiduciaries of the plan who, (2) while acting within their capacities as plan fiduciaries, (3) engaged in conduct constituting a breach of an ERISA fiduciary duty.")

# Fiduciaries are per se prohibited from...

- Self dealing – providing advice that will increase the compensation paid to the advisor, his/her supervising firm and/or any affiliate(s);
- Dual representation – acting on behalf of or representing a party dealing with the plan in a transaction involving the assets of the plan; or
- Third party payments – receiving any consideration for his/her own personal account from any party dealing with the plan in connection with a transaction involving the assets of the plan.

# A fiduciary must act...

*"with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims."*

See ERISA 404(a)(1)(B)

# Regarding investments fiduciaries...

*Must give “appropriate consideration” to those facts and circumstances that... the fiduciary knows or should know are relevant to the particular investment or investment course of action involved, including the role the investment or investment course of action plays in that portion of the [client's] investment portfolio with respect to which the fiduciary has investment duties.*

*See 29 CFR 2550.404a-1*

# To defend a claim, fiduciaries must ...

*Demonstrate "the individual trustees, at the time they engaged in the challenged transactions, employed the appropriate methods to investigate the merits of the investment and to structure the investment."*

*Fiduciaries' prudence is measured against an objective standard, and their own "lack of familiarity with investments is no excuse" for failing to act with the care, skill, prudence and diligence required under the circumstances then prevailing.*

# Early claims alleged liability for ...

- failing to take into account revenue-sharing fees paid by mutual fund managers to record keepers and other vendors;
- offering mutual funds as investment options instead of lower cost separate accounts or collective trusts;
- offering more expensive actively managed funds as investment options instead of index funds; and
- offering more expensive retail class mutual funds as investment options instead of institutional class funds.



# Recent cases expanded theories to ...

- failing to properly monitor record-keeping fees;
- offering low-cost index funds was imprudent for large plans that could have qualified for cheaper share classes;
- universities and other nonprofits' 403(b) plans included too many funds or more than one record keeper, and thus did not minimize fees and expenses by using economies of scale; and
- the plan's record keepers received excessive compensation based on fees paid for “robo advisers” that advise plan participants.

# Investment-related claims include:

- actively managed funds underperformed against relevant benchmarks;
- hedge funds and private equity investments should not have been included in target date and diversified funds;
- stable value funds were too conservative and underperformed against benchmarks; and
- stable value funds should have been offered instead of money market funds as an investment option.

# Breach of loyalty argued fiduciaries...

(1) "favor[ed] the financial interests of TIAA-CREF in receiving a steady stream of revenues from bundled services over the interest of participants" (Count I)

(2) "allow[ed] TIAA-CREF and Vanguard to put their proprietary investments in the Plans without scrutinizing those providers' financial interest in using funds that provided them a steady stream of revenue sharing payments" (Count III); and

(3) failed to consider the conflicts associated with offering the recordkeepers' own proprietary investments in the Plans (Count V).

# Failure of loyalty counts I, III and V ...

Count I - allowing providers to include proprietary funds without considering potential conflicts -- **allegations do not include facts suggesting that defendant entered into the transaction for the purpose of (rather than merely having the effect of) benefitting the provider.**

Count III – allowing providers to include proprietary investments "without scrutinizing those providers' financial interests that provided them a steady stream of revenue sharing payments" -- **is a claim that NYU followed an imprudent process—not that it acted disloyally.**

Count V - "[a]ll of the Plans' options were the recordkeepers' own proprietary investments." -- **does not support an inference that defendant failed to act solely in the interest of participants.**

# Claims relating to prudence include...

- (1) Entering into/extending “lock-in” arrangement that required the plans to include/retain particular investments/providers (Count I);
- (2) Excessive fees from failing to: i) solicit bids from other recordkeepers; ii) monitor recordkeeping revenue sharing and fees generally; and iii) determine whether the plans should use a single recordkeeper.(Count III); and
- (3) Losses caused by: i) continuing to offer two RK prop. funds with high fees/poor performance; ii) including poorly performing, actively managed, retail funds; iii) investments w/ unnecessary layers of fees; and iv) failing to consolidate the plans (Count V).

# Failure of prudence counts I, II and V...

Count I – entering into/extending lock-in arrangements – **locked-in funds only = 2% of options; contract to include those investments does not, by itself, demonstrate imprudence—plaintiffs have not demonstrated that it resulted in retaining "plainly risky" options; and a contract that restricts ability to seek less expensive service providers, standing alone, does not breach duty of prudence.**

Count III – procedural deficiencies relating to soliciting bids, excessive fees and consolidation of RKs ***survived initially, but after trial the court held “the Committee prudently managed its recordkeepers: it ran prudent RFP processes, was able to obtain lower fees ... when consolidation was not deemed prudent, and it consolidated recordkeepers [for one plan].”***



# Failure of prudence counts I, II and V...

Count V – challenge to specific funds and poor performance ***survived initially, but share class and failure to consolidate lineups did not --*** when retail funds are just several of a wide range of options, courts have held that their inclusion was not imprudent and the low fees associated with these particular retail options indicates their inclusion does not demonstrate an unwise choice; no facts to suggest that the Plans' beneficiaries were harmed by offering numerous choices.

After trial, the court held that performance was closely monitored by Cammack and that, at least some of the fiduciaries, were engaged in deciding to retain such investments.

## Notable quotes:

- *“assertions that alternative recordkeepers—with whom [the plan] was allegedly precluded from contracting—could have provided “superior services at a lower cost” ... “does not [alone] support imprudence. If it did, the mere entry into the market of a lower-cost and superior provider would lead to a breach of fiduciary duty.”*
- *“whether fees are excessive or not is relative to the quality of services provided. In other words, under [case law], in certain circumstances, paying more for superior services might be more prudent than paying less for inferior ones.”*
- *“While revenue sharing is a ‘common industry practice,’ a fiduciary's failure to ensure that ‘recordkeepers charged appropriate fees and did not receive overpayments for their services’ may be a violation of ERISA.”*

## Notable quotes:

- *“even if plaintiffs had established that NYU did not follow a prudent process in monitoring administrative fees and investments, in order to be entitled to recover damages, the Plan(s) must have also suffered a causally related loss.”*
- *“The hiring or appointment of a co-fiduciary does not relieve the original fiduciary of its independent duties; no fiduciary may passively rely on information provided by a co-fiduciary. A fiduciary who delegates fiduciary responsibilities nonetheless retains a duty to exercise prudence “in continuing the allocation or designation.”*
- *“In order to rely on an expert’s advice, a ‘fiduciary must (1) investigate the expert’s qualifications, (2) provide the expert with complete and accurate information, and (3) make certain that reliance on the expert’s advice is reasonably justified under the circumstances.’”*

## Notable quotes:

- *After trial, “the Court does not view the existence of the Cammack recommendations, and any failure to follow those recommendations, as strong evidence of imprudence. Indeed, it demonstrates Committee decision-making independent of Cammack.”*
- *“NYU believed any recordkeeper switch could not be completed without risk of significant errors or additional changes prior to completion of this global update of NYU’s systems and technology... Thus, until the other system updates were completed, it would not have been prudent for the Committee to consolidate recordkeepers.”*

# Notable quotes:

- “[Dir. of Benefits] testimony was concerning. She made it clear that she viewed her role as primarily concerned with scheduling, paper movement, and logistics; she displayed a surprising lack of in-depth knowledge concerning the financial aspects of managing a multi-billion-dollar pension portfolio and a lack of true appreciation for the significance of her role as a fiduciary.” She testified that “[i]t’s not my job to determine whether the fees are appropriate” for the Plans.”
- [Top HR Official] testified that:
  - she did not “know enough about variable annuities to be able to comment on whether they should be in these plans,”
  - When asked who the plan administrator was, she responded, “I don’t review the plan documents. That’s what I have staff for.”

ERISA requires fiduciaries to follow a prudent process when selecting, monitoring and/or replacing investments. Sec. 404(c) protects fiduciaries who offer a “broad range” of diversified Designated Investment Alternatives (DIAs).

If participants are automatically enrolled, fiduciaries must designate appropriate Qualified Default Investment Alternatives (QDIAs).

## INVESTMENTS

A small icon of a bar chart with an upward-pointing arrow, indicating growth or investment.

### EVALUATION

- How much help do participants need in planning and investing for retirement?
- What behaviors do participants exhibit regarding risk tolerance, withdrawal patterns, etc.?
- What is the appropriate number/type of investment options to make available to participants?
- What criteria should govern the process for selecting, monitoring, and replacing DIAs and QDIAs, model portfolios and investment managers, if applicable?

### OUTPUT

Documentation of information reviewed and basis for decision to select, monitor and replace investments.

## FIDUCIARY FILE

A small icon of a folder with a downward-pointing arrow, indicating a file or document.



Fiduciaries are required to make informed decisions when selecting, monitoring and replacing service providers. Sec. 408(b)(2) requires all “covered” service providers to disclose certain information, including a description of the services and all direct and indirect compensation received.

To avoid entering into a prohibited transaction, fiduciaries must evaluate this information, prior to selection and periodically thereafter, to ensure the services are necessary and terms and compensation are reasonable.

## SERVICE PROVIDERS

### EVALUATION

- What are the needs of the plan/participants?
- Are participants satisfied and are services utilized?
- What is the experience and background of the service provider?
- How is the service provider compensated?
- Are there any potential/actual conflicts of interests that may affect the judgment of the service provider?
- Is the compensation received reasonable in light of the value of the services provided?

### OUTPUT

Documentation of information reviewed and basis for decision to select/retain service provider.

## FIDUCIARY FILE

Fiduciaries are responsible for ensuring that the plan is properly administered and certain notices, disclosures and forms are provided to participants and regulators. The 408(b)(2) disclosures should contain the data necessary to prepare disclosures to participants under 404a-5 and for completing the Form 5500 and Schedule C, if applicable.

Fiduciaries should be familiar with the plan document and create a process to oversee eligibility and vesting. The plan advisor may assist by coordinating service provider assistance.

## ADMINISTRATION & REPORTING

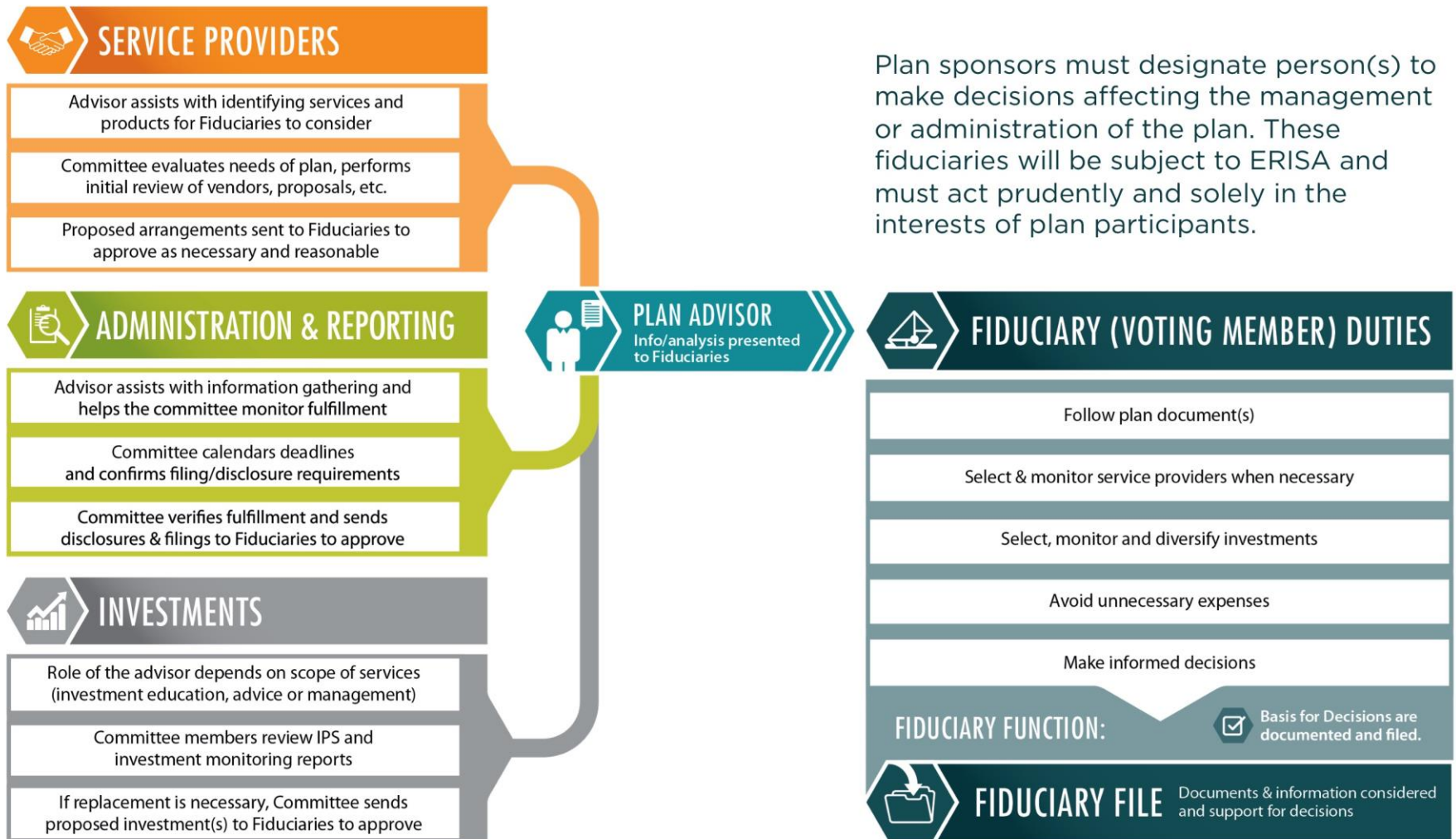
### EVALUATION

- What are the policies concerning, and who is responsible for approving, loans and distributions, and who will ensure contributions are deposited?
- What notices, forms and/or disclosures are required to be provided to participants and at what frequencies?
- What records will be used to reconcile information required to determine eligibility and vesting?
- Who is responsible for preparing, approving and distributing notices, disclosures and filings?

### OUTPUT

Copies of all required notices, disclosures and filings and any supporting information and/or notes.

## FIDUCIARY FILE







## EXAM-READY FIDUCIARY FILE



### INVESTMENTS

#### Investment Policy Statement (IPS)

Copy of IPS

#### Reporting

- Investment Selections and Monitoring Reports
- Model Portfolio Allocation and Performance Reports
- Other Investment Reports and Research
- 3(38) Investment Fiduciary Selection and Monitoring Material and Reports

#### Committee Meetings

- Meeting Minutes
- Documentation Resulting From Action Items



### ADMINISTRATION & REPORTING

#### Plan Documents

- Plan Document (With Amendments & Restatements)
- Trust Document
- Summary Plan Description (SPD)
- Determination Letter(s)
- Delegations of Fiduciary Duty

#### Notices

- Benefits Statements
- Notice of right to diversify out of employer securities
- 404(c); Auto Enrollment/QDIA; 404a-5 (Annual); & Blackout

#### Bonding & Insurance

- Copy of: Fidelity Bond; Fiduciary Liability Policy; Etc.

#### Service Provider Agreements

- Custodial; Investment Advisor; Recordkeeping; Etc.

#### Participant Communications

- Enrollment Records
- Beneficiary Designations
- Contribution Elections
- Employee Meeting Attendee Lists
- Distribution Records
- Proof of 404a-5 Notice Distribution

#### Discrimination Testing

- Testing Records

#### Regulatory Filings

- 5500 & Other Financial Statements & Filings

#### Committee Meetings

- Meeting Minutes
- Documentation Resulting From Action Items



### SERVICE PROVIDERS

#### Plan Needs Analysis

- Documentation of plan and participant needs

#### Requests for Proposal (RFP)

- Compiled Results
- Provider Proposals

#### Fee Disclosure Statements

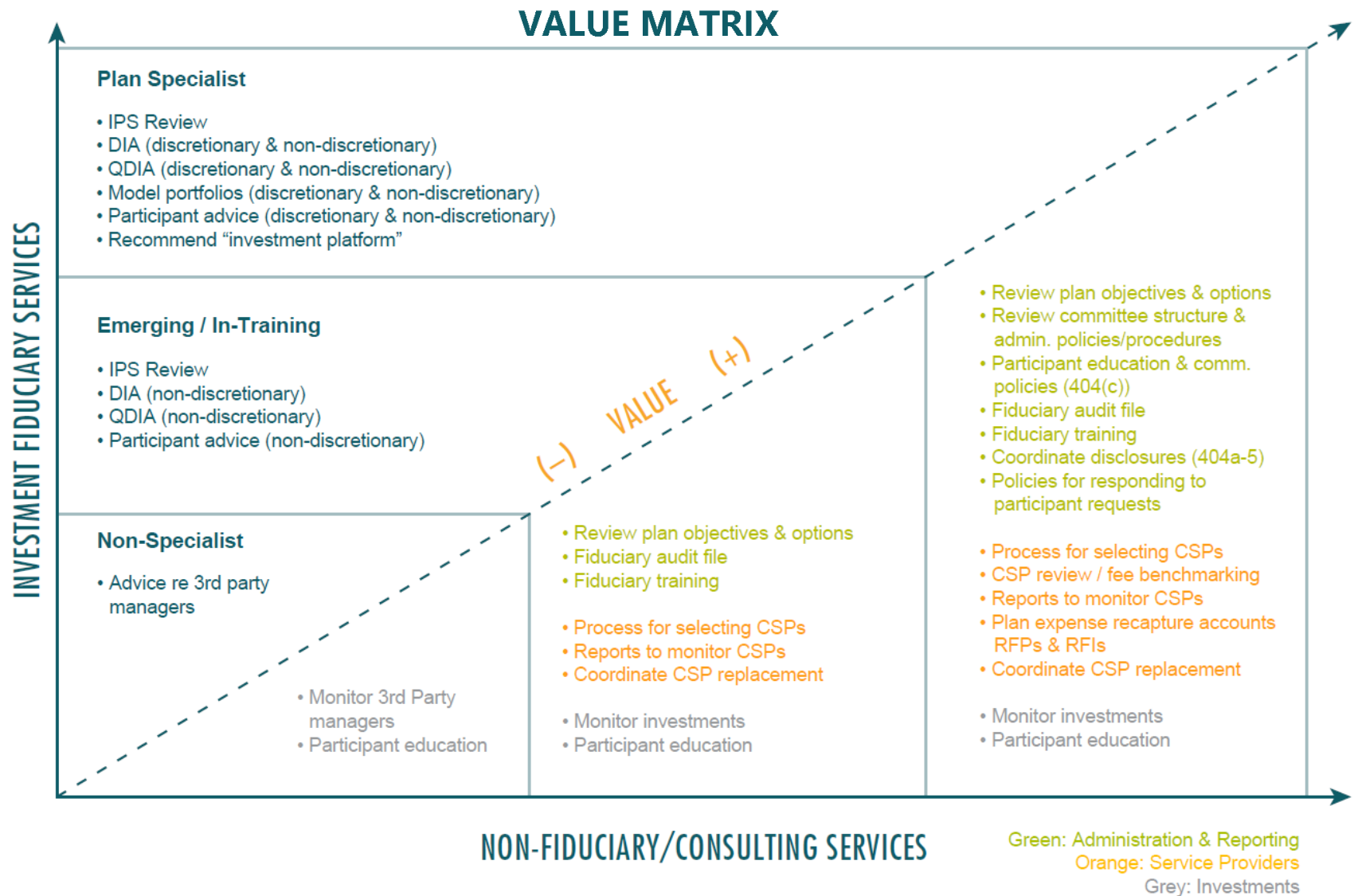
- 408(b)(2) Fee Disclosure Reports

#### Benchmarking & Performance Analysis

- Benchmarking Reports
- Fee & Service Reviews

#### Committee Meetings

- Meeting Minutes
- Documentation Resulting From Action Items





# SAMPLE NEEDS ASSESSMENT WORKSHEET

	VERY IMPORTANT	IMPORTANT	NOT IMPORTANT / UNSURE
REVIEW OF OBJECTIVES AND OPTIONS AVAILABLE THROUGH THE PLAN?			
COMMITTEE STRUCTURE AND ADMINISTRATIVE POLICIES?			
PARTICIPANT COMMUNICATION AND EDUCATION POLICIES?			
DEVELOPMENT AND MAINTENANCE OF FIDUCIARY AUDIT FILE AND DOCUMENT RETENTION?			
FIDUCIARY TRAINING FOR PLAN COMMITTEE?			
ASSISTANCE WITH SELECTING, MONITORING AND REPLACING SERVICE PROVIDERS?			
REVIEW OF COVERED SERVICE PROVIDER DISCLOSURES AND FEE BENCHMARKING?			
REVIEW OF REPORTS TO MONITOR SERVICE PROVIDERS?			
ASSISTANCE WITH OVERSEEING PLAN EXPENSE ACCOUNTS?			
PREPARATION AND REVIEW OF REQUESTS FOR PROPOSALS?			
REPLACEMENT AND CONVERSION OF SERVICE PROVIDER?			
DEVELOPMENT OF INVESTMENT POLICY STATEMENT?			
INVESTMENT EDUCATION AND GUIDANCE?			
INVESTMENT RECOMMENDATIONS OR ADVICE?			
DISCRETIONARY INVESTMENT MANAGEMENT?			
GENERAL FINANCIAL WELLNESS AND RETIREMENT PLANNING?			
ENROLLMENT SUPPORT AND INVESTMENT EDUCATION AND GUIDANCE?			
INVESTMENT RECOMMENDATIONS OR ADVICE?			
DISCRETIONARY INVESTMENT MANAGEMENT?			

## FOR MORE INFORMATION:



**PENSION-RESOURCES.COM**

*Additional G-MAP compatible resources available  
at: <https://portal.pension-resources.com>*

*[info@pension-resources.com](mailto:info@pension-resources.com)*

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