



## Employee Benefits & Executive Compensation ADVISORY ■

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### ERISA Fiduciary Decisions – Making Changes to Your Qualified Plan’s Investment Lineup

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From time to time, fiduciary committees need to consider whether to make a change in the investment alternatives available in their retirement plans. Typically in 401(k) and 403(b) plans and sometimes in other defined contribution plans, the fiduciary committee selects the investment options or funds available in the retirement plan (the investment lineup). Participants and beneficiaries then select among the various investment alternatives and designate a percentage of their account balance that will be invested in their chosen investment funds.<sup>1</sup>

There are multiple reasons that could prompt a fiduciary committee to consider making changes in their retirement plan’s investment lineup. Poor performance, eliminating duplicate and overlapping funds, expanding investments alternatives, organizational changes at the fund manager level, significant changes in amount of assets under management, evaluation of fees, etc., are all potential reasons for considering investment alternative changes. As an example, recent financial news regarding changes at the PIMCO Total Return Fund has prompted some of our clients to ask us about the process of evaluating investment funds.<sup>2</sup> Regardless of the reason for considering a change, this advisory summarizes the technical requirements and recommended procedures in making changes to your plan’s investment lineup.

#### **Step One: Review the Investment Policy Statement**

Investment Policy Statements (IPS) frequently contain specific qualitative and quantitative criteria for selecting and monitoring investment funds. The first step in considering changes in an investment lineup is to be aware of the IPS and its guidelines. Not all plans have an IPS, but if an IPS has been adopted, it is important to adhere to the IPS and any procedures set forth for considering changes to investment alternatives. If current concerns are not reflected in the IPS’s criteria, we recommend amending the IPS to cover appropriate criteria.

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<sup>1</sup> Fiduciary committees generally designate a default investment option if a participant fails to make an election. The Department of Labor has established criteria that if met, will result in the participant or beneficiary being treated as if he or she made an affirmative investment election (known as a Qualified Default Investment Alternative).

<sup>2</sup> See, for example, <http://www.reuters.com/article/2014/11/04/us-pimco-allianz-outflows-idUSKBN0IO29320141104>; <http://www.latimes.com/business/la-fi-pimco-gross-funds-20141105-story.html>; <https://investments.pimco.com/Products/Pages/346.aspx>.

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## Step Two: Exercise Prudence in the Selection and Monitoring of the Investment Lineup

If certain procedural requirements are followed, ERISA Section 404(c) may provide plan fiduciaries with some protection against losses resulting from investment decisions made by plan participants. However, there is some controversy as to whether ERISA Section 404(c) shields plan fiduciaries from liability for claims regarding the imprudent offering of plan investment options themselves. In other words, the choice of which investment alternatives are available under a retirement plan is an ERISA fiduciary decision for which ERISA Section 404(c) may not be a complete shield. When a significant event occurs that affects an investment alternative offered under the plan, it is advisable for plan fiduciaries to consider whether any actions are necessary in response to the event. We advise plan fiduciaries to engage in a reasoned decision-making process, consistent with ERISA Section 404(a)'s prudent man standard of care.

The prudent man standard of care focuses on the process by which the plan fiduciaries make their decisions, rather than the specific results of those decisions. Courts considering whether plan fiduciaries meet the prudent man standard will ask whether a fiduciary employed the appropriate methods and process necessary to investigate and determine the merits of a particular investment alternative.

When a significant event occurs, plan fiduciaries should consider holding a meeting to discuss whether changing an investment option available under the plan or any other actions are necessary in response to the event. Some events may prompt a special meeting that occurs before a fiduciary committee's regularly scheduled quarterly or semiannual meeting. Any such meeting should also include discussion regarding the plan fiduciaries' prudent process, which may include:

- Reviewing the potential consequences stemming from the significant event;
- Recapping the investment fund's past performance and fees compared to alternative investment funds;
- Seeking the advice of outside consultants or legal professionals regarding the significant event and the investment fund's potential for future performance;
- Discussing the pros and cons of keeping vs. changing the investment fund; and
- Reviewing the IPS (see above) and adhering to procedural guidelines set forth therein for evaluating plan investment alternatives.

By undergoing a prudent process, plan fiduciaries will be better protected from any breach of fiduciary duty claim alleging actions that should have been taken in response to the significant event.

## Step Three: Document the Decision

The meeting and discussion described in step two should be documented in writing. Maintaining committee minutes or other documentation of committee discussions helps the committee prove it met its ERISA fiduciary standards and responsibilities. This is especially important when the committee reaches a decision either to change an investment alternative under the plan or to keep an investment alternative, if there has been a significant event affecting that investment alternative. The reasons supporting the decision (including the key factors discussed) should be reported in the documentation.

## Step Four: Inform Participants of the Change

Once the fiduciary committee has determined that it is necessary to replace or eliminate an investment alternative under the plan, it is important to consider participant notification requirements. These may put limitations on the fiduciary committee's ability to make a rapid fund change. These requirements arise under ERISA Section 404, which has two separate notification requirements:

- Section 404(a)-5 requires disclosure to participants related to fees for designated investment alternatives under the plan. Any change to the lineup of designated investment alternatives will generally require notice to participants at least 30 days in advance of such a change. The regulation contains an important exception in the event of circumstances beyond the control of the plan administrator, in which case advance notice is required as soon as reasonably practicable.

- The regulations provide that voluntary use of Section 404(c) protection requires at least 30 days' advance notice of changes in investment options. There is no exception to this notice requirement, although it is unclear how a court would view this requirement in a case of exigent circumstances. Compliance with ERISA 404(c) is not mandatory, though compliance offers fiduciary protections regarding the mapping and investment of participant accounts.

### **Step Five: Continue to Monitor Investment Lineup**

Regardless of the fiduciary committee's decision on whether to make a change to a given investment alternative under the plan, the fiduciary committee should continue to monitor all investment alternatives and the overall investment lineup. Fiduciary committees normally carry out these monitoring activities through regular committee meetings, but, as noted above, when a significant event occurs, a special meeting may be necessary to ensure fiduciary standards are met.

### **Conclusion**

Changes in investment lineups occur from time to time. Fiduciary committees should follow a prudent process in considering investment changes in their retirement plans.

Please do not hesitate to contact your Alston & Bird attorney if we can assist you in this process.

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