

ERISA Plan Investment Committee Governance: Avoiding Breach of Fiduciary Duty Claims

Evaluating Fiduciary Risks and Litigating Alleged Breaches by Investment Committee Members

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Today's faculty features:

Dr. Susan Mangiero, **Fiduciary Leadership**, Trumbull, Conn.

Rhonda Prussack, V.P., Fiduciary Liability Product Manager,
Berkshire Hathaway Specialty Insurance, New York

Richard Siegel, Esq., **Alston & Bird**, Washington, D.C.

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Description

- One of the best techniques a plan sponsor can implement to avoid fiduciary risk is the installation of an effective investment committee. Sponsors must take care in establishing protocols to **ensure the committees operate within strict ERISA standards.**
- One of those strict standards is the “prudent expert” standard. This standard is higher than that of the typical fiduciary. Also, investment committee decisions must comply with the “exclusive benefit rule.” ERISA counsel must be prepared to **create and implement specific processes** to ensure that each and every decision is made within these constraints and more.
- Attendees will benefit from a discussion of risk mitigation techniques to minimize the probability that allegations of breach of fiduciary duty will be made. This includes selection, training and review protocols as well as the role of ERISA fiduciary liability insurance coverage.
- This program will also address some litigation strategies should litigation occur.

Speaker Bio – Susan Mangiero, PhD, AIFA, CFA, FRM, PPC



- Dr. Susan Mangiero is a managing director with Fiduciary Leadership, LLC and is a CFA charterholder, certified Financial Risk Manager, Accredited Investment Fiduciary Analyst™ and Professional Plan Consultant™.
- She has provided testimony and behind-the-scenes forensic analysis, calculation of damages and rebuttal report commentary for various investment governance, investment performance, fiduciary breach, prudence, risk and valuation matters.
- She has over 20 years of experience in capital markets, global treasury, asset-liability management, portfolio management, economic and investment analysis, derivatives, financial risk control and valuation. This includes work on trading desks for several global banks, in the areas of fixed income, foreign exchange, interest rate and currency swaps, futures and options.
- She is a frequently invited speaker and has keynoted or led workshops for organizations such as the Stable Value Investment Association, Harvard Law School, AICPA - Employee Benefits Section, National Association of Corporate Directors and Financial Executives International.
- Susan can be reached at susanm@fiduciaryleadership.com or (203) 261-5519.

Speaker Bio – Rhonda Prussack



Ms. Rhonda Prussack is Vice President, Fiduciary Liability Product Manager at Berkshire Hathaway Specialty Insurance. Rhonda has 24 years of insurance industry experience and has developed and brought to market state-of-the-art fiduciary liability policies and coverages for corporations, organized labor, municipalities, and not-for-profits. Early in Rhonda's career she had roles at Dean Witter, Johnson & Higgins, and the New York City Employees' Retirement System. Rhonda has written articles for and been quoted in many publications, and is a frequent speaker at ERISA and executive liability seminars around the U.S. and Canada.

Rhonda received her B.A. from Brooklyn College.

Reach Rhonda at rhonda.prussack@bhspecialty.com or 917-960-2449.

Speaker Bio – Richard Siegel, Esq.



- Richard Siegel is a senior associate in the ERISA Litigation Group of the Washington, D.C. Alston & Bird LLP, where his practice focuses on various labor, employment, employee benefits and ERISA litigation matters.
- Richard’s ERISA and employee benefits litigation experience includes counseling and representing plan sponsors and fiduciaries in litigation on the numerous duties imposed upon fiduciaries in the administration of plans and investment of plan assets, including the prudent selection and oversight of investment professionals and other service providers, prohibited transaction issues, interpretation of plan documents, unfunded and underfunded liabilities, withdrawal liability and claims for benefits.
- In addition, Richard frequently represents employers in various aspects of labor and employment law, and other complex civil litigation.
- Richard can be reached at richard.siegel@alston.com or 1-202-239-3696.

Investment Committee Governance:

Best Practices and Hot Button Issues

Susan Mangiero, PhD, AIFA, CFA, FRM, PPC
Managing Director
Fiduciary Leadership, LLC

Investment Fiduciary Issues

- I. Increased Scrutiny of Core Issues
 - A. Compensation
 - B. Conflicts of Interest
 - C. Delegation of Duties
 - D. Allocation of Duties

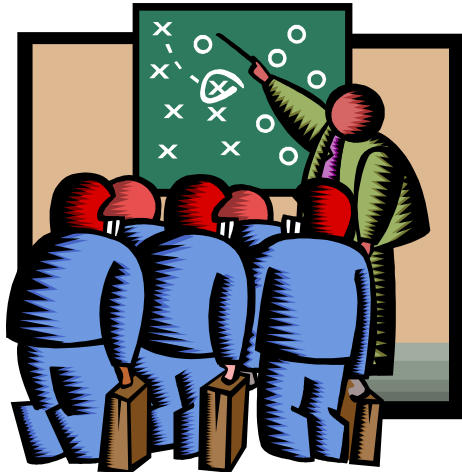
- II. Nature of Liability
 - A. Individual
 - B. Collective
 - C. Professional
 - D. Personal

- III. Use of Third Parties
 - A. Outsourced Chief Investment Officer
 - B. Fiduciary Risk Management
 - C. Functional But Not Contractual

Regulatory Focus – Partial List

ERISA Advisory Council	<u>Outsourcing Employee Benefit Plan Services</u>
U.S. Department of Labor	<u>Fiduciary Service Provider Compensation Project</u>
U.S. Securities and Exchange Commission	<u>Regulation of Investment Advisers</u>
<i>Pensions & Benefits</i> , Joe Lustig, October 11, 2013	<u>DOL Investigators Quiz Plan Sponsors On Training of Fiduciaries, Attorneys Say</u>
U.S. Government Accountability Office	<u>Conflicts of Interest Can Affect Defined Benefit and Defined Contribution Plans</u>
<i>Wall Street Journal</i> , Dan Fitzpatrick, June 8, 2014	<u>Pension Advisers Need a Closer Look</u>

Committee Selection Process



Disciplined Approach or Random?

Qualification Considerations

- I. Experience
 - A. Investment Management
 - B. Corporate Finance
 - C. Human Resources
 - D. Operations

- II. Knowledge
 - A. University Degree(s)
 - B. Certification(s)
 - C. Minimum Year Requirement
 - D. Continuing Education

- I. Role With Plan Sponsor
 - A. Director or Officer
 - B. Risk Manager
 - C. HR Administration
 - D. Legal

*No Shortage of Certifications**



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* Some certifications focus on the broader investment management arena.

Investment Committee Reviews

I. Purpose

II. Content

III. Regularity

IV. Compensation

V. Turnover

*Investment Committee Documents**

- I. Charter
 - A. Roles and Responsibilities
 - B. Support Staff
 - C. Use of Consultants
 - D. Nature of Delegation

- II. Investment Policy Statement
 - A. Risk Tolerance
 - B. Time Horizon
 - C. Constraints
 - D. Plan Design
 - E. Leverage
 - F. Liquidity
 - G. Asset Category Limits

* Partial List

Other Investment Committee Documents to Consider

III. Vendor Procedures

- A. Open or Closed
- B. Specificity of Scope of Work
- C. Qualitative Factors
- D. Quantitative Factors

IV. Risk Management Statement

- A. Securities Lending
- B. Derivatives
- C. Short Selling
- D. Margin
- E. Technology
- F. Trading Limits
- G. Valuation Policies and Procedures

Investment Committee Charter Purpose and Duties: Example

I. Purpose:

The Retirement Plan Investment Committee (RPIC) provides investment oversight for the Seattle University Employees Retirement Plan (Plan), including policies and practices and the performance of the Plan's investment vehicles.

II. Fiduciary Responsibility

The Plan is subject to the Employee Retirement Income Security Act of 1974, as amended (ERISA), including its fiduciary provisions. The University is the Plan's named fiduciary and has authority to manage and control the Plan's operation and administration. RPIC members also are fiduciaries with respect to the Plan to the extent they perform fiduciary functions described in ERISA Section 3(21)(A). A fiduciary's duty to monitor the Plan's investments is important and failure to satisfy that or other fiduciary duties may trigger significant liability, including the fiduciary's personal liability under ERISA. Recognizing this and to the extent permitted by applicable law, the University has agreed to indemnify and hold harmless RPIC members for any alleged breach of fiduciary duty with respect to the Plan, except in the case of the fiduciary's gross negligence or willful misconduct.

Source: [Seattle University Website](#)

Investment Committee Charter Management and Tasks: Example

III. Authority and Responsibilities

The RPIC's operating authority and responsibilities, as determined by the University, include:

- Establishing, periodically reviewing, and maintaining a written investment policy, including investment allocation strategies.
- Reviewing and monitoring investment performance, including the reasonableness of investment fees, against appropriate benchmarks and in accordance with the investment policy.
- Managing the Plan to ensure regulatory compliance pertaining to Plan investments, including required Plan amendments and document retention.
- Selecting and monitoring recordkeeping of the investment institutions offered in the Plan's operations.

Investment Committee Charter

Tasks – More: Example

- Monitoring for reasonableness and consistency with the Plan's terms any investment product fees and assessments passed through to Plan participants.
- Retaining counsel or consultants as needed to advise the RPIC.
- Reporting to the President and the Finance Committee of the University's Board of Trustees regarding investment policy changes or performance concerns.
- Overseeing administration of the Plan in accordance with the Plan's investment policy, including:
 - Selecting an appropriate number and type of investment asset classes and management styles for Plan participants, including for default investment elections.
 - Establishing performance criteria and benchmarks for selected asset classes.
 - Researching, selecting, and withdrawing Plan investments as appropriate for specified asset classes or styles.
 - Reviewing communication methods and materials to ensure that Plan participants receive adequate investment education and performance information.
 - Monitoring Plan investment costs.
 - Ensuring the RPIC and the Plan comply with applicable laws, regulations, and the terms of the Plan pertaining to investments.
 - In coordination with the University's offices of Finance and Human Resources, reviewing the Plan's annual independent financial audit.

Investment Committee Charter Composition and Timing: Example

IV. Committee Membership and Meetings

A. The RPIC will be comprised of the following members:

- Chief Human Resources Officer (Chair)
- Chief Finance Officer
- Dean of Business School
- Economics or Finance faculty member or similarly qualified employee

The RPIC's voting members are chosen and can be removed by the University's Board of Trustees. Additionally, the RPIC Chair may appoint up to four at-large members to serve in an advisory capacity to the RPIC. The at-large members will be selected based on specific relevant expertise and/or as representatives of the University's faculty and staff. The at-large members will not have any authority to vote in the RPIC's decisions.

All RPIC members will acknowledge in writing and on an annual basis their membership in the RPIC.

B. The RPIC will have scheduled regular meetings with authority to convene additional meetings as deemed necessary or advisable by the Chair. A quorum for the transaction of business at any RPIC meeting shall be a majority of the RPIC members. Decisions shall be made by a majority of those present at the meeting.

The RPIC will invite at-large members to scheduled meetings and external advisors or others as deemed necessary or advisable by the Chair. The RPIC may hold private meetings with retirement investment consultants and meet in executive session as needed or advisable by the Chair.

Investment Committee and Vendors

- I. Establishing Needs
 - A. Investment Strategy
 - B. Investment Style
 - C. Standalone or Integrated
 - D. Staffing

- II. Contracting
 - A. RFP
 - B. Fees
 - C. Due Diligence
 - D. Termination

Some Resources and Articles

“Plan Governance Toolkit” - TIAA-CREF

Best Practices for Investment Committees by Rocco DiBruno and Donald B. Trone (Wiley, July 2007)

“Formation of the Investment Committee,” fi360

“Unsticking the status quo: The role of diversity in investment committee effectiveness” by Catherine D. Gordon, Vanguard, May 2014

“Meeting your Fiduciary Responsibilities” United States Department of Labor

“Establishing an Investment Committee for Your Company’s Retirement Plan,” RBC Wealth Management, 2014

ERISA Fiduciary Insurance:

Impact of Investment Committee Composition

Rhonda Prussack
VP and Fiduciary Liability Product Manager
Berkshire Hathaway Specialty Insurance

Coverage Under the Policy

- What are the policies designed to cover?
- Who is insured under the policy?

Defense Provision

- Duty to Defend
- Non-Duty to Defend
- Combination

What is Not Covered

- Typical Exclusions
 - Conduct
 - Prior notice
 - Pending or prior litigation
 - Prior acts
 - Discrimination
 - Failure to fund
 - Pollution
 - Benefits
- Other Insurance

Indemnification

- Presumptive indemnification
- Is indemnification available?
- ERISA Section 410 - Exculpatory Provisions
- “...any provision in an agreement or instrument which purports to relieve a fiduciary from responsibility or liability for any responsibility, obligation, or duty under this part shall be void as against public policy.”
- *Johnson v. Couturier* (9th Cir. July 27, 2009)

Demonstrating Low Risk

- Prudent processes
- Composition of plan investment committee
- Training
- Written investment guidelines

ERISA Litigation:

Investment Committee Liability and Defense Tactics

Richard Siegel, Esquire
ERISA Litigation Group
Alston & Bird LLP

An Ounce of Prevention . . .

The best defense is a good offense

Document decisions

- Not just the what, but the why

Litigation Tactics

Experts

Class Certification

Lessons learned from recent cases

Expert Witnesses

Prudence Expert

Investment Expert

Damages Expert

- May be same as investment expert

Class Certification – Rule 23(a)

Numerosity

Commonality

Typicality

Adequacy

Class Certification – Rule 23(a)

Attacking Commonality

- *Wal-Mart Stores, Inc. v. Dukes*, 131 S. Ct. 2541 (2011)
- Will there be common *answers*, not common *questions*?
- Highlight differences in claims among putative class.
 - *i.e.*, Different risk tolerance, different fees paid, etc.

Class Certification – Rule 23(a)

Attacking Typicality

- Based upon the named plaintiffs
- Fact-specific
- Discovery may support
- How do lead plaintiffs claims differ from the class claims?

Class Certification – Rule 23(a)

Attacking Adequacy

- Plaintiffs and/or Counsel
- Fact-specific
- Based on discovery
- Possible issues
 - Conflicts with class
 - Personal knowledge
 - Counsel experience

Class Certification – Rule 23(b)(3)

Common questions of law or fact predominate over questions affecting individual members.

- Other issues present even if commonality exists? Example - Statute of limitations

Class action is superior.

- Size of the class?
- Which law?
- Fee-shifting

Lessons Learned – Recent Cases

Tussey v. ABB, Inc., 746 F.3d 327 (8th Cir. 2014)

Tibble v. Edison International, 711 F.3d 1061 (9th Cir. 2013)

Fifth Third Bancorp. v. Dudenhoeffer, 134 S. Ct. 2459 (2014)

Tussey v. ABB, Inc.

One of the first fee cases to go to trial

Bad facts → Bad law

- Defendants made no effort to benchmark the fees being paid.
- Defendants were warned by a consultant that plan fees were subsidizing corporate fees.
- No evidence that defendants attempted to use purchasing power (\$1.4B) to reduce fees.
- Failure to follow plan documents & obtain revenue sharing rebates

Tussey v. ABB, Inc.

But investment selection judgment reversed

- Defendants had replaced default investments.
- District court:
 - Defendants failed to follow process required by plan documents.
 - Had they done so, they would not have changed investments.
- 8th Circuit:
 - District court improperly applied *de novo* review in deciding proper investments.

Tibble v. Edison International

- Affirmed finding for defendants on all claims except with regard to purchasing retail-class, rather than institutional-class alternatives.
- District Court held and Ninth Circuit affirmed that fiduciaries failed to ensure that reliance on investment advise was reasonably justified.
- Not reasonably justified because committee “reflexively and uncritically adopt[ed] investment recommendations.”

Tibble v. Edison International

- “[A]n utter absence of evidence that Edison considered the possibility of institutional classes.”
- “[B]ecause the goal is not to duplicate the expert’s analysis, had Edison made a showing that HFS engaged in a prudent process in considering share classes, this might have been a different case.”

Tibble v. Edison International

“Edison did not present evidence of: the specific recommendations HFS made to the Investments Staff regarding those funds, what the scope of HFS's review was, whether HFS considered both the retail and institutional share classes or what questions or steps the Investments Staff [pursued] to evaluate HFS' recommendations.”

Fifth Third Bancorp v. Dudenhoeffer

What about when investment committees have responsibilities for employer stock?

Prior to *Fifth Third*, if plans either required or (strongly) encouraged the offering of company stock, every circuit held fiduciaries were subject to a presumption of prudence.

- Plaintiffs would have to plead that, under the circumstances, plan settlor would not have intended that plan terms would be followed.

Result: Almost all cases dismissed

Fifth Third Bancorp v. Dudenhoeffer

Fifth Third: No presumption of prudence.

- Other than with respect to diversification, ERISA's duty of prudence applies equally to ESOP fiduciaries as all other fiduciaries.

Result: Investment committees will no longer be able to simply rely on language of plan requiring offering of company stock.

Fifth Third Bancorp v. Dudenhoeffer

Much still to be resolved with *Fifth Third*. Supreme Court appears to have severely limited the types of allegations that will state a plausible claim.

- If based on public allegations, presumption that stock price has accounted for this.
- If based on non-public allegations, deference to insider trading laws (and spirit of laws).

Although more lawsuits likely, post-*Fifth Third world* may be no better for plaintiffs.