"I don't need fiduciary insurance… I am not a fiduciary."

By Chris Williams

"*I don't need fiduciary insurance. I am not a fiduciary. We have a third party vendor take care of all that stuff for us*." For agents that sell fiduciary liability insurance, this is a common refrain from clients.

In a survey conducted by Alliance Bernstein, 37% of respondents were not even aware they were fiduciaries. The fact that an individual is not named in a plan document does not mean that person is not a fiduciary. Under the Employee Retirement Income Security Act of 1974 ("ERISA"), a federal law which established rules for managing employee benefit plans, whether an individual is a fiduciary is determined based on the functions he or she performs in the organization, and not their title. A fiduciary is someone who:

- Exercises discretionary authority over plan administration. Plan administration includes setting policies and procedures for the benefit plan.
- Exercises discretionary authority over benefit plan management . Plan management is responsible for implementing the policies and procedures.
- Has any authority or control over benefit plan assets. This includes selecting investments and outside service providers.
- Provides investment advice for a fee.

If an individual performs any of those functions for a benefit plan, they will be deemed a fiduciary. ERISA imposes certain obligations on fiduciaries:

- Under the exclusive benefit rule, fiduciaries must discharge their duties solely in the interest of plan participants and for the exclusive purpose of providing benefits to plan participants and defraying reasonable expenses of administering the plan.
- Under the prudent man rule, fiduciaries must act with the care, skill, prudence and diligence that a prudent person acting in a similar situation would exercise.
- Fiduciaries have an obligation to diversify investments to minimize the risk of large losses.
- Fiduciaries have an obligation to follow the terms of the plan document.

The failure of a fiduciary to perform those duties can result in personal liability. What does that mean? First, the benefit plan is legally prohibited from indemnifying the fiduciary. Second, if a plaintiff prevails in their claim against a fiduciary, they can seek to recover damages, and their attorney fees, from the fiduciary's personal bank account!

Some employers operate on the misunderstanding that they can transfer all their fiduciary responsibilities to a third party. This simply is not the case. An organization can certainly hire a third party fiduciary to manage investments, establish policies and procedures, and implement those procedures, but the employer can never completely escape liability.

Section 405(c) of ERISA allows a plan fiduciary to delegate its fiduciary responsibility to a third party, but the fiduciary can never completely escape liability. A plan fiduciary can still be held liable for making the decision to allocate fiduciary responsibility to a third party; failing to establish a procedure to prudently select a third party; or continuing to use a third party. Thus, even if a company has an investment manager who assumes fiduciary responsibility, the company and its fiduciaries can still be sued for 1) selecting the investment manager; 2) failing to establish a procedure to prudently select that investment manager, or 3) failing to monitor the investment manager. While Section 405(c) of ERISA can provide some protection, there is no guarantee or immunity from lawsuits by plan participants. If the investment manager is sued, the prudent plaintiff's lawyer will likely sue the plan fiduciaries as well.

Consider the following real life example. Thomas Perez, the United States Secretary of Labor, filed suit against a company and two employees who were fiduciaries. The company hired an investment manager who had complete authority over the plan assets. The investment manager invested the plan assets in a limited number of large energy stocks.   The investments were subsequently sold for cash. Secretary Perez argued alleged the fiduciaries breached their duties by failing to monitor the investment manager.

In short, ERISA imposes significant obligations on plan fiduciaries. ERISA does not allow them to shift all their responsibilities to a third party. For those that neglect those duties, the cost of a claim can be significant. For that reason, the trusted advisor will guide their clients on the benefit of fiduciary liability insurance, which covers companies, their directors, officers, and employees for breaches of fiduciary duties.