

What's your fiduciary liability IQ?

If it needs to be raised, and it probably does, just follow these steps.

BY CHRISTINE DART

ALL IT a ripple effect of America's economic slump. Companies are facing increasing risk of fiduciary liability lawsuits from disenchanted employees who are seeing their retirement benefits diminished, their employer matching contributions eliminated, or their benefits reduced or terminated.

If the overall economic impact on investment returns isn't enough to make plaintiff attorneys cheer, regulatory and legal changes have also helped land today's fiduciaries in the hot seat. Changes in the laws governing employee benefit plans such as the Employee Retirement Income Security Act (ERISA), the Pension Protection Act of 2006, the Consolidated Omnibus Budget Reconciliation Act (COBRA), and the Health Insurance Portability and Accountability Act (HIPAA), make it even more challenging for fiduciaries to navigate. In addition, the U.S. Supreme Court ruling in 2008 in *LaRue v. DeWolf* makes it easier for current and former employees to sue fiduciaries.

Despite the increased exposure, fiduciary liability is often a misunderstood risk for boards in some small to midsize firms. Boards that are responsible for appointing ERISA fiduciaries to oversee their companies' benefit plans are also responsible for monitoring those appointed to serve in that capacity. If board members fail in these responsibilities, they can be held personally liable if a court finds them in violation

of their fiduciary trust. Directors and officers should take steps to minimize their exposure and improve their ability to defend themselves in the event of a lawsuit.

The increased exposure comes from many sources. In recent years more employees and former employees have filed lawsuits alleging the plan fiduciaries breached their duty under ERISA by offering employer securities in the plan, failing to diversify plan assets, calculating benefits incorrectly, wrongfully terminating a plan, or failing to disclose revenue-sharing arrangements and excessive fees.

Sometimes lawsuits arise when a company conducts a series of voluntary employee layoffs. If during the latter part of the layoffs, the company enhances the benefit level to encourage employees to leave, the company could be liable for claims alleging it knew it would initiate a series of layoffs over time and that the subsequent layoffs would come with enhanced benefits.

Employee layoffs can also increase exposure to "breach of fiduciary duty" allegations concerning severance or pension benefit calculations, including ERISA Section 510 claims for interference of a participant's rights under a qualified plan. Even when a participant decides not to take any legal action against the plan fiduciaries, the U.S. Department of Labor, which monitors corporate compliance with ERISA, may decide to take plan fiduciaries to court over alleged breaches of their fiduciary duties.



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The U.S. Supreme Court's *LaRue v. DeWolf* decision makes it easier for individuals to sue over alleged breaches of fiduciary duty. The high court ruled that an individual participant in a defined-benefit contribution plan could sue to recover losses to the participant's individual account. In doing so, the Supreme Court vacated the decision of the Court of Appeals for the Fourth Circuit that held Section 502(a)(2) remedies were only available for the plan as a whole, and not to the individual participants. In addition, the Supreme Court has determined that former participants of a plan may have standing to sue if they have a "colorable" claim — a claim that need not be actually true, but is strong enough to have a decent chance of being valid — for additional benefits. This will make it easier for plaintiff firms to attract those participants who are no longer employed with the company to file a lawsuit.

Bankruptcies may also increase fiduciary liability exposure. If in a bankruptcy the Pension Benefit Guaranty Corp. assumes the responsibility for an underfunded pension plan, it does not guarantee 100% of the participant's benefits. Nor will a bankruptcy filing protect deferred-compensation plan benefits, as participants must stand in line with all other creditors in the bankrupt company's estate. Either scenario is likely to increase exposure to litigation from participants in those plans.

No company, director, or fiduciary can completely avoid the risk of legal action, but directors can take steps to mitigate their companies' fiduciary risk in several ways, including:

- *Have a Process:* Make sure your company has a solid fiduciary process in place. Be sure the benefit plan's fiduciary structure and the plan documents are in synch with how the plan is actually managed. The fiduciary process should include continuing education to ensure that the fiduciaries are familiar with the plan documents and kept up to date of any changes in the plan. Fiduciaries also should have a policy for replacing the investment manager if necessary. Taking no action may also expose fiduciaries to

greater risk of litigation.

- *Know the Law:* Fiduciaries need to stay abreast of the laws that govern employee benefit plans. Having an ongoing education program to assist in this area is highly recommended. Fiduciaries need to be intimately familiar with the duties required of them under ERISA and to avoid any prohibited transactions that might arise.

- *Document Decisions and Responsibilities:* Typically the investment committee or administrative committee of a plan will report periodically to the board of directors who are responsible for monitoring and may also be responsible for appointing the fiduciaries of the plan. It is important that the committee members selected have the time and expertise to properly perform their fiduciary duties. All meeting minutes should be documented thoroughly, including matters considered, decisions made, actions taken, and recommendations received from outside service providers. Keep in mind, however, that plaintiff attorneys will be sure to review these documents for evidence of a fiduciary breach. Also important is that fiduciaries may delegate responsibility to a registered investment advisor, bank, or qualified insurance company, but only if the investment manager recognizes in writing its fiduciary status. Once their

status is on file, it should be reviewed and updated annually to avoid liability for the investment advisors acts or omissions.

- *Monitor Benchmarks:* Fiduciaries have a responsibility to monitor the company's benefit plans. It is therefore wise to have benchmarks in place as part of a comprehensive policy governing

Consider purchasing a fiduciary liability policy to protect yourself in situations where the company may become insolvent.

investments and asset allocation. Fiduciaries should review the policy at least quarterly to see how the plans match up against the benchmarks. And at least once a year they should monitor plan fees, expenses, and charges to ensure the costs are reasonable and plans are not charged expenses that should be paid by the plan sponsor.

- *Communicate:* Companies should inform their employees promptly when any changes are made in their benefit

plans. Before employers reduce or freeze benefits, or eliminate them entirely, they should make sure their benefit plan documents allow for those moves.

- *Maximize Protection:* A corporation's bylaws should provide for indemnification of fiduciaries to the fullest extent permitted by law. In addition, the fiduciaries should consider purchasing a fiduciary liability policy to protect themselves in situations where the employer may become insolvent or the bylaws amended to restrict indemnification. In addition, a periodic review should be made of any 404(c) plan, to ensure it is in compliance with all provisions, in order that plan fiduciaries may shield themselves from liability related to individual investment choices made by benefit plan participants.

- *Consult Legal Counsel:* Directors should also confer with a qualified attorney, not only to review plan documents but also to make recommendations to further strengthen the company's fiduciary process.

Taking these prudent steps will help employers, directors, officers, and fiduciaries reduce their risk of litigation — and help them defend themselves when lawsuits arise. ■

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