



# Where IT and Fiduciary Responsibility Meet

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# Basic Terminology

- Settlor** = the creator of the trust  
(state or local government)
- Trustees** = board that oversees the trust
- Participants** = covered employees, retirees
- Beneficiaries** = employees entitled to a benefit,  
retirees, & spouses/dependents
- Fiduciaries** = trustees, investment managers,  
and others (IT professionals?)

# Basic Terminology

**Service providers** = outside entities that provide services to the plan (IT may engage many plan service providers)

**ERISA** = Federal law (administered by DOL) that applies to non-public, corporate and union sponsored plans

**Public Plan** = A state plan or other local government plan

# Trust Law Evolution

- Old English law recognized trusts
- Family trusts have existed for centuries
- Pension funds emerged in the 1900s
- ERISA codified pension trust law in 1974
  - Public plans are not subject to ERISA
  - But ERISA is extremely influential
  - Public plan laws are modeled after ERISA
  - Public plans trustees look to ERISA for guidance

# Why is it important to know if you are a fiduciary?

- Fiduciaries must satisfy very high standards of conduct
- Under ERISA, fiduciaries may become personally liable for violating those standards of conduct
  - Applicable state or local law may be different
- Fiduciaries often obtain fiduciary liability insurance coverage

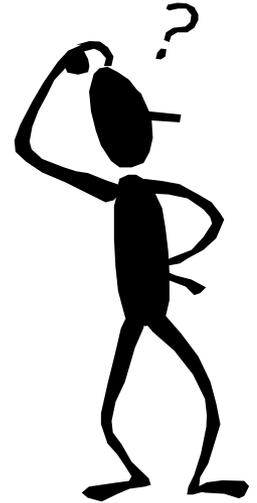
# Are you a fiduciary?

- ERISA has a “functional” definition:
  - You are a fiduciary if your job involves a “fiduciary function” (regardless of what is in your job description)
  - Even if your job does not involve a fiduciary function, you are a fiduciary if take on a fiduciary function (*i.e.*, act outside your job)
  - Ministerial acts are not fiduciary functions
- Applicable state/local law may be different

# What is a fiduciary function?

- If you exercise discretionary authority or control with respect to management of the plan or the assets of the plan  
*or*
- If you actually have discretionary authority or responsibility for plan administration  
*or*
- If you provide investment advice for a fee

# Can an IT professional be a fiduciary?



- Does the ERISA model apply?
- Do you hire and fire plan service providers?
- Do you buy products from vendors?
- Do you have discretionary authority or responsibility for plan administration?
- You might be a fiduciary with respect to some parts of your job, but not others...

# What if you are not a fiduciary?

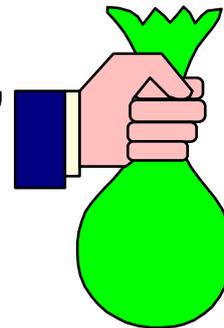
- If you are not a fiduciary, then another manager (your boss?) or the trustees will have fiduciary responsibility for the IT function
- Therefore, if you are not a fiduciary – good news – you might not risk personal liability
  - But your boss may be personally liable for a fiduciary breach if you perform poorly

# Fiduciary Duty of Loyalty

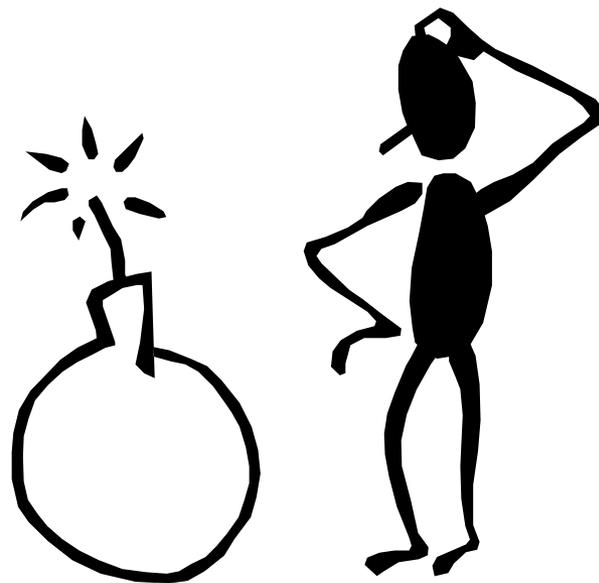
- Most public plans have this concept
- Fiduciaries must discharge their duties solely in the interests of participants and beneficiaries
- For the exclusive purposes of:
  - providing benefits to participants/beneficiaries
  - defraying reasonable administrative expenses
- No duty of loyalty to legislature, taxpayers

# Fiduciary Self-Dealing & Conflicts

- Self-dealing – cannot act in a transaction if the fiduciary has a self-interest (e.g., hiring a relative’s firm to be a service provider)
- Cannot represent a party with an adverse interest (e.g., negotiate a contract on behalf of a service provider)
- Cannot accept a “kick-back”

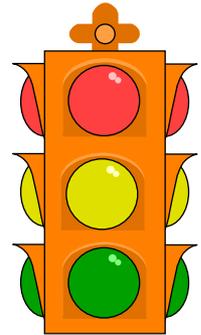


Can you  
accept a ham  
for Hunakkah  
from a  
plan service  
provider?



# Resolving Fiduciary Conflicts

- Avoid if possible
- Disclose and recuse if unavoidable
  - Very technical, tenuous conflicts may be okay
  - Recusal means absence from all consideration
- No way to resolve a kick-back
  - Disclosure and recusal are not a remedy for kick-backs



# Fiduciary Duty of Prudence

- Most public plans have this concept
- Prudent expert standard
- Must act with the care, skill, prudence and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of like character and with like aims
- Pure heart and empty head does not work

# Public Plans = the *least* fiduciary latitude

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Public Plans

Prudent Expert/Public Scrutiny

Corporate & Union ERISA Plans

ERISA Prudent Expert

Not for Profit Organizations

Prudent Person

Corporate Board of Directors

Business Judgment Rule

# Satisfying the Prudence Standard

- Procedural prudence –
  - (1) consider appropriate facts and circumstances and (2) act accordingly
- May require consulting with experts (either on staff, or outside consultants)
- Judged at the time the transaction is entered – not in hindsight
- A prudent process is more important than a good outcome

# Fiduciary liability



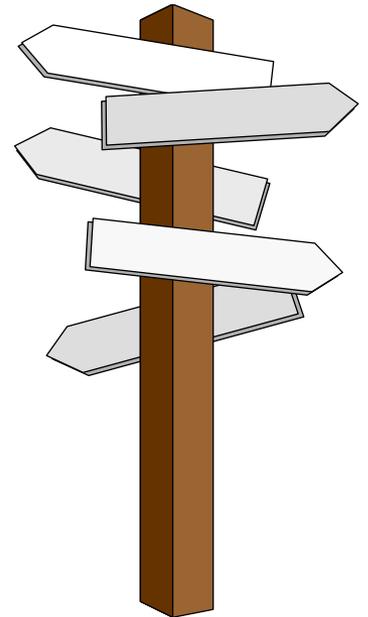
- You are your brother's keeper
- If you know of another fiduciary's breach and do nothing, you will breach your own fiduciary duty
- Resigning, without more, is not a solution

# Delegating Fiduciary Duties

- Generally, fiduciaries can delegate responsibilities
- But the ultimate responsibility (liability) remains with the fiduciary
  - If the trustees delegate the contracting function to IT, you may *share* the fiduciary responsibility (liability) with the trustees
- Fiduciaries have a duty to monitor delegees and replace them if appropriate

# Exercising Loyalty & Prudence

- Comply with applicable law & plan policies
- Monitor those who carry out duties
- Exercise procedural prudence
- Consult experts as appropriate
- Avoid or resolve conflicts



# Protection From Liability

- Rely on experts (not always)
- Procedural prudence (might be a safe harbor)
- Government or sovereign immunity (probably not)
- Fiduciary liability insurance (to a limited extent, may be covered under the plan's policy)

# Plan Expenses

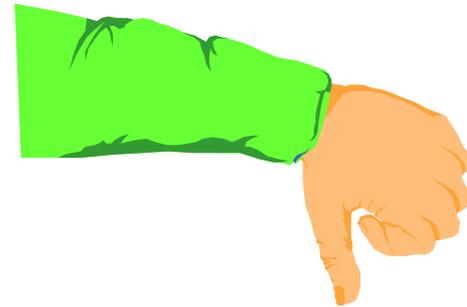
- Expenses must relate to services for which the plan is authorized to pay under governing plan documents
- The services must be “appropriate” for the plan
- The amount paid must be “reasonable”
- Arrangement must not involve fiduciary self-dealing, conflicts, or kick-backs

# Appropriate Services

- Generally, any cost incurred by fiduciaries can be paid from plan assets
- For example
  - Plan administration expenses, recordkeeping, participant communications, actuarial and accounting fees, claims processing fees
  - Fees for trust and custodial services
  - Investment expenses

# *Not* Appropriate Services

- Services benefiting the employer (*i.e.*, settlor services)
- Services to a different plan or third party other than the plan
- Services not reasonably necessary to carry out plan administrative, investment and operational requirements

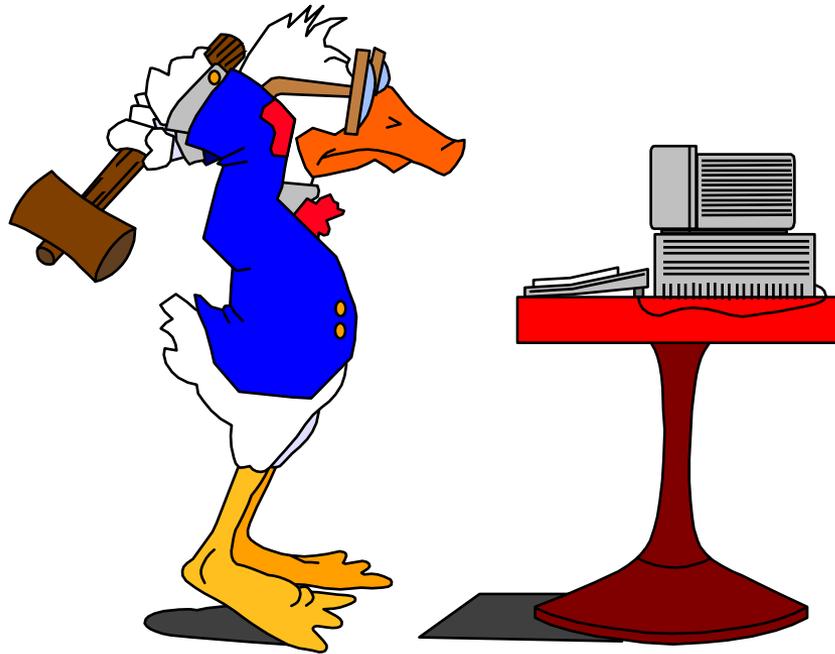


# *Reasonable* in Amount

- Reasonableness must be determined in light of the services rendered
  - As would ordinarily be paid for like services by like enterprises under like circumstances
  - Within the range of compensation to others in the same industry or occupation for similar services
- Reasonableness is measured at the time the contract is entered
  - Not at the time the contract is questioned



# IT Issues



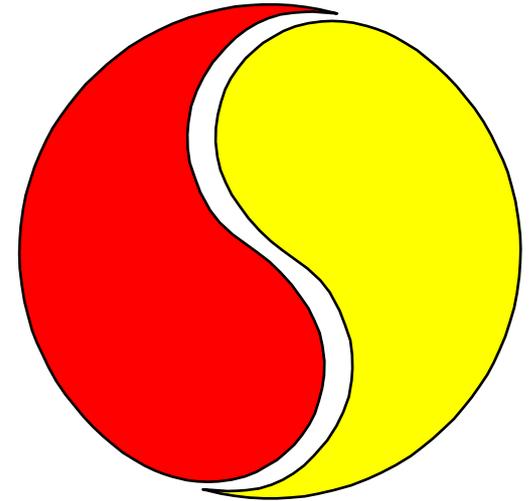
# Are you making a fiduciary decision when you purchase an admin system?

- Reportedly, up to 1/3 of the administrative budget is spent on IT
- Some spend \$25M on admin systems
- Considerations:
  - What is IT's role?
  - Are you wearing your fiduciary hat?
  - Is the cost reasonable?



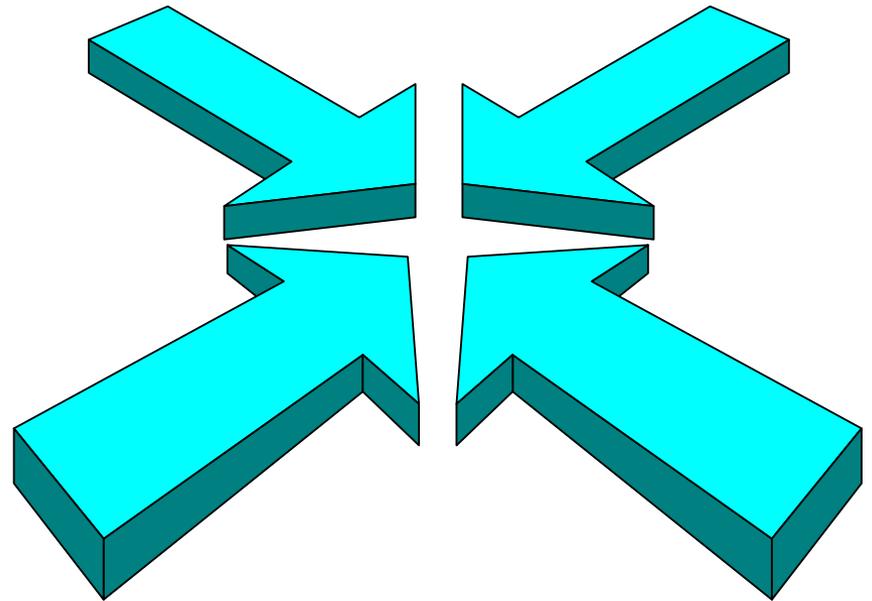
# Service Delivery

- One end of spectrum – Bare Bones
  - Is it okay to provide poor service to save dollars?
- Other end – the Cadillac
  - Can you purchase a Cadillac admin system to service 10 participants?
- What are the fiduciary issues?

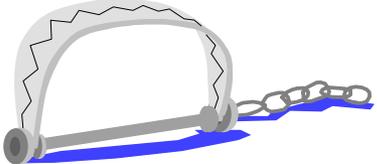


# Consolidating IT

- Some states want to consolidate the IT function across all state agencies
- Is standardization through consolidation good for everyone?



# Consolidating IT

- Are you acting “solely in the interest” of plan participants and beneficiaries?
- Privacy or confidentiality issues? 
- Are plan funds being used to either pay benefits or defray reasonable plan administrative expenses?

# Consolidating IT

- Is this an expense that benefits a party other than the plan?
- Are you subsidizing the state government “*have nots*” in the guise of standardization?
- Securities law issues?
  - Insider trading concerns?
  - Does the plan’s system contain confidential investment information that might be compromised?



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