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Sponsors Need More Guidance On Outsourcing Services: ERISA Council

By Mary B. Andersen, CEBS, ERPA, QPA



As it's become routine for employee plan sponsors to shift their recordkeeping to service providers outside the company, keeping sight of their fiduciary responsibility while outsourcing has become more important than ever.

In recognition of this, the 2014 ERISA Advisory Council on Employee Welfare and Pension Benefit Plans chose as one of its topics for examination for the year employee benefit plan outsourcing, focusing specifically on functions historically performed by plan sponsors. The council, which consists of benefits industry and participant representatives, was established under ERISA Section 512 to provide guidance to the U.S. Department of Labor on matters related to welfare and pension benefits.

The council's report, issued in January, said the council aimed to identify areas where DOL could provide education, outreach and regulatory guidance for plan sponsors about their responsibilities when outsourcing. To gather this information, the council held two days of public hearings with plan sponsors, attorneys, service providers, academia and DOL staff.

The council's report provides recommendations in these areas:

- educating plan sponsors on current outsourcing trends;
- clarifying ERISA's rules for delegating responsibility to service providers;
- providing additional guidance on the selection and monitoring of service providers;
- facilitating the use of multiple employer plans to encourage retirement plan formation and to ease related administrative burdens; and

- giving additional guidance on insurance coverage and bonding of outsourced services.

This column will analyze how some of these issues affect retirement plan sponsors.

Selecting and Monitoring Service Providers

Selecting a service provider is a fiduciary act because it involves the exercise of discretionary authority or control over the management and administration of a plan. The decision to retain or remove a service provider is also a fiduciary act. Once a service provider is appointed, the plan sponsor has a fiduciary duty to monitor the performance of the plan's "trustees and other fiduciaries," including those hired outside the company to provide plan services.

Recommendation: *The report indicated that more guidance from federal regulators is needed in the area of measuring service providers' performance. Beyond investment management, there isn't much guidance for plan sponsors in this area, and a more coordinated approach to monitoring would be useful, the council concluded. While available guidance is good, the council believes it could be refreshed, especially in the area of fiduciary services such as recordkeeping.*

Plan sponsors have learned that selecting a service provider is an important yet time-consuming endeavor. Unless the plan sponsor has available internal resources, a consultant experienced in service provider searches is often retained. The service provider search begins by carefully thinking about what it is that a plan sponsor is looking for in a service provider. The plan sponsor should begin by reviewing the services it currently receives and asking: Is anything missing? All interested parties at the plan sponsor should be included in this review as part of an evaluation and selection committee.

Activities of the company that are critical to the success of the retirement plan (for example, human resources,

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payroll, finance, systems) should be represented on the committee. This committee will work closely with any retained search consultant. It should identify prospective service providers to include in the request for proposals process.

The current service provider should be included in the RFP, unless the plan sponsor has come to the conclusion that the provider cannot provide either the quality or level of service needed. These would include plan provisions that do not fit a prototype, more hands-on assistance or more consulting.

Together with the search consultant, an RFP is prepared, potential service providers are identified and an evaluation matrix is developed. The consultant will compile the results and review them with the committee for its ultimate selection of a service provider. It is imperative that the selection process be documented.

The plan sponsor's responsibilities do not end with the selection. Ongoing monitoring is critical. In fact, such monitoring should be part of the agreement with the service provider. Monitoring can include performance measurements (for example, participant statements delivered on time, participant calls to vendor's Customer Service line answered within prescribed time frames, reviews of investment performance and fee competitiveness). Monitoring activities should be documented.

Measuring performance and fees is often accomplished through a periodic service provider search, but that is a major undertaking. Benchmarks exist to compare plan expenses to similar-sized plans, but not all plans are alike.

DOL has provided guidance on selecting and monitoring service providers through several publications available on the DOL's website (Tips for the Selection and Monitoring of Service Providers for Your Employee Benefit Plan [<http://www.dol.gov/ebsa/newsroom/fs052505.html>], Meeting Your Fiduciary Responsibilities [<http://www.dol.gov/ebsa/publications/fiduciaryresponsibility.html>] and Selecting and Monitoring Pension Consultants — Tips for Plan Fiduciaries [<http://www.dol.gov/ebsa/newsroom/fs053105.html>]). Testimony to the ERISA Advisory Council in 2014 indicated that questions from the second publication have become an industry standard in connection with investment consulting RFPs.

Multiple Employer Plans

A MEP is a retirement plan in which two or more unrelated employers participate. (The health and welfare plan equivalent is a multiple employer welfare arrangement, or MEWA). The participating employer signs an agreement to join the MEP, and the MEP administrator is responsible for the MEP's operations. The participating employer provides demographic information for the participants as well as ongoing plan information such as salary and years of service.

Multiple Employer Plans

Recommendation: *The council said in its report that it believes that MEPs have merit, and recommends that DOL consider how to make the existing rules work, especially in cases where a MEP can be used to provide retirement income for employees without employer-sponsored retirement plans. The council's recommendations for this area included: (1) developing safe harbors for employers that would enable them to avoid liability for another employer in the MEP; and (2) developing something akin to a prototype or standard MEP, which would provide the necessary structure to avoid conflicts of interest, prohibited transactions and fiduciary concerns.*

As a reminder, a MEP can be open or closed. A closed MEP requires that there be a "common nexus or other genuine organization relationship that is unrelated to the provisions of benefits" between the lead sponsor and the participating employers. (Note: This differs from a multiemployer plan, which is formed through a collective bargaining agreement and usually covers employers in the same industry).

An association is an example of a closed MEP. An open MEP is just as it sounds, open to various employers that are not part of a group or association. Open MEPs are not treated as a single plan, but rather as an aggregation of single plans, each with its own plan sponsor. A closed MEP is treated as a single plan for ERISA purposes. As a result, the employer is not responsible for filing the annual Form 5500 or for plan administration activities.

However, a barrier to greater use of MEPs in plan outsourcing is the lack of clarity about the individual plan sponsor's responsibility, should one of the participating plan sponsors fail to meet their obligations,

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namely by not contributing to the plan. ERISA provides that such a failure imposes a liability on the remaining employers, a provision that makes MEPs less attractive for potential employer members.

Outsourcing has many advantages including access to the latest technology, legal and compliance assistance and help mitigating plan sponsor fiduciary risk, in that the third-party administrator has the processes and manpower many plan sponsors don't have to perform plan functions.

However, it is not unusual for plan sponsors to believe that their fiduciary responsibility is outsourced along with plan administrative or investment functions. Some service providers will assume limited fiduciary duty with respect to specific functions (for example, QDRO administration). Often the service provider is merely following agreed-upon procedures developed jointly by the plan sponsor and the service provider. It is important to understand who is doing what and what fiduciary responsibility, if any, the service provider is assuming.

We will hear more on the definition of fiduciary when the long-awaited regulations (see November 2011 column) are issued as expected this year.

Take-aways for Plan Sponsors

1. If you are interested in a MEP, make sure you know what you are getting into when you sign the adoption agreement. Retain an experienced MEP consultant to take you through the decision process.
2. As you have heard many times before, document, document, document any outsourced functions. Understand who is doing what. Develop a process to periodically review promises made in the outsourcing agreement.
3. Watch for updated federal regulatory fiduciary guidance.
4. Regularly visit the DOL website for information. ❖

Mary B. Andersen is president and founder of ERISAdiagnostics Inc., an employee benefits consulting firm that provides services related to Forms 5500, plan documents, summary plan descriptions and compliance/operational reviews. Ms. Andersen has more than 25 years of benefits consulting and administration experience. She is a CEBS fellow and member of the charter class. She has also achieved the enrolled retirement plan agent designation and has been a frequent speaker on compliance-related issues. Ms. Andersen is the contributing editor of Thompson's Pension Plan Fix-It Handbook.



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