

Fiduciary Best Practices: Helping You Meet Your Obligations under ERISA Part Three: Failure to Perform Fiduciary Duties, is there a Problem?

By Mike Rogers, Director of Retirement Services

What happens if you fail in your role as a fiduciary? As my dad used to say, “We have a carrot but we also have a stick.” Failure to comply is a stick that can be quite large and thorny. If you don’t carry out your responsibilities, fail to follow all of the appropriate rules, or take actions counter to your role, you are considered in breach of your fiduciary duties.

ERISA holds fiduciaries personally liable for losses in the Plan if they fail to perform their fiduciary duties.

Personal Liability: The extension of personal liability usually comes as a shock to fiduciaries. Individuals on 401(k) or investment committees have personal liability while serving in these roles. We recommend that you check your E&O or D&O policies to see if they extend coverage to fiduciaries. If they do not, there is now a specialty line of insurance for fiduciaries which have very reasonably priced premiums, given the levels of coverage.

Prohibited Transactions: Certain acts as a fiduciary may result in what are called “Prohibited Transactions.” These come with a 15% penalty which is cumulative over multiple years. For example, failure to submit payroll contributions timely is technically a Prohibited Transaction. Something that happened year ago may spiral into an issue that may span multiple years until corrected. This can result in relatively large penalties for what might be deemed a simple administrative oversight.

Civil Penalty: More severe breaches may result in a 20% penalty. These penalties are not deductible by the plan sponsor and may not be paid by the assets of the plan. One of the most common instances of this is failure to have the required audit of the form 5500 or failure to file a form 5500.

Criminal Sanctions: For even more severe breaches, criminal sanctions may be imposed. The most typical example of this is when the plan fiduciaries, instead of sending participant 401(k) contributions to the Plan, divert these funds for other uses. There is actually a daily email sent out which highlights such transactions, which refutes the belief that “any publicity is good publicity.”

Disqualification of the Guilty Party from Ever Serving as a Fiduciary under ERISA: In addition to the above items, if a fiduciary is found guilty of a breach, they can be barred from ever serving in a similar role in the future. This announcement is typically accompanied by a large press release announcing not only the company name but the names of the fiduciaries in question. There are several recent examples of individuals who actually received jail sentences for egregious transactions.

While the above items may seem daunting, at least under ERISA, fiduciaries cannot be held liable for punitive damages.

Next, I will focus on ways to reduce this fiduciary liability and properly create a corporate governance structure to alleviate liability.

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