VOLUME 73 ◆ NUMBER 6

Employee Benefit Plan Review

Top 10 Areas of Focus in DOL Investigations of Retirement Plans

BRIAN J. DOUGHERTY AND ELIZABETH S. GOLDBERG

The U.S. Department of Labor (DOL) has been extremely active in recent years as the federal agency investigating and enforcing the fiduciary duties under the Employee Retirement Income Security Act of 1974, as amended (ERISA). These investigations have continued to result in findings of fiduciary breach and monetary recoveries for ERISA retirement plans.

In light of this active enforcement program and the resulting recoveries, retirement plan administrators should consider a compliance self-review, including on the issues that the DOL appears to focus the most. To that end, this article identifies the top 10 issues of DOL focus with respect to retirement plan fiduciary compliance. This list is a reminder of the importance of a proactive self-review by plan administrators, even before the DOL initiates an investigation.

1) Terminated Vested Participants that are Missing or Have Not Commenced Benefits at Required Beginning Date

The DOL has put significant resources since 2015 into examinations of whether defined benefit plan administrators are adequately searching for missing participants; notifying deferred vested participants that are past the plan's "normal retirement age" to commence their payable retirement benefit; and encouraging participants (especially unresponsive participants) to commence benefits on time (namely by the plan's "required beginning date"). This is a significant focus of current DOL enforcement activities and recoveries. This area can be challenging for plan administrators because there is no directly applicable guidance on the fiduciary standards that apply in ongoing plan administration or for defined benefit plan administration, although related guidance can be instructive, such as the Department of Labor Field Assistance Bulletin 2014-01, which provides guidance on searches for missing participants in terminating defined contribution plans.

The enforcement initiative is also evolving, more of these investigations are being opened, and being opened out of more regional offices. These investigations are also evolving in scope, such as into the new topic of uncashed check procedures and examinations of defined contribution plans.

2) Timeliness of Participant Contributions

The DOL has long had a focus on protecting employee contributions into both retirement plans and contributory health plans. The DOL is particularly focused on making sure these contributions go into the plan (in the first place, and on time). Participant contributions are treated as plan assets, and therefore must be deposited

into the plan as of the date they can reasonably be segregated from the employer's general assets. This standard will vary from plan to plan, but DOL guidance interprets this "reasonable segregation" time as at least the 15th business day of the month following the month of withholding. Informally the DOL has stated that it expects this window to be much smaller than 15 days, such as three days. There is also a seven-day safe harbor for small plans.

Part of the DOL's focus also includes reviewing whether participant loan repayments are paid into the plan, including during times of inactive services (such as leaves of absence).

Findings of breach related to the timeliness of contributions make up a high proportion of all DOL enforcement findings (by number). In egregious cases where, for example, there is intentional theft or misuse of employee contributions, the DOL will (working with the U.S. Department of Justice) treat the matter as a criminal investigation.

3) Required Plan Documents and Disclosures

The DOL will always evaluate a plan to confirm that there is the proper maintenance of required documents and the dissemination of required disclosures. This includes the maintenance and/or disclosure of such documents as the plan's summary plan description, participant level disclosures (i.e., the 404a-5 disclosure), the receipt of plan service provider disclosures (i.e., the 408(b)(2) disclosure) and other disclosures covered by Title I of ERISA, such as blackout notices for investment or service disruptions, and mapping notices, if the plan is seeking 404(c) protection when it changes the plan's investment options.

If the DOL finds gaps in a plan's required documents, it will typically focus on encouraging the plan administrator to fix those gaps. However, in egregious cases, the DOL may impose statutory penalties for the failure to provide such disclosures (or maintain required documents).

4) Bonding

The DOL will almost always request evidence of a plan's bond. ERISA Section 412 generally requires that every plan fiduciary and every person who handles plan assets be bonded for at least 10 percent of the amount of funds he or she handles, up to a maximum of $500,000 per plan ($1 million for plans that hold employer securities). The bond must protect the plan from the theft of plan assets.

When the DOL discovers that a plan lacks a bond, it will require that a bond be obtained before closing the investigation.

5) Plan Fiduciary Processes and Claims Procedures

The DOL will often review a plan to confirm that the plan is processing claims in accordance with the DOL claims regulations (which set minimum time lines and disclosures for the processing of claims and appeals). Although this issue arises more frequently with respect to health plans, the DOL also reviews retirement plans to confirm compliance with its claims regulations. For example, the DOL routinely asks for recent claims and appeals and reviews those materials against the requirements of its claims regulations. For that reason, care should be taken to implement a program to comply with those regulations, and document such compliance, when handling participant claims and appeals.

Although not necessarily required under ERISA, the DOL will also examine whether a plan operates with certain documents and structures that it views as "best practices" to achieve compliance with ERISA's fiduciary standards. These include a plan investment policy statement, a fiduciary or trustee committee, regular committee meetings, and minutes from the plan's named fiduciary (i.e., the fiduciary committee). The DOL will often view the lack of such documents or structures as probative of an inadequate fiduciary process (even though the law may not require these documents or structures). Moreover, in cases where there are other facts establishing a possible fiduciary breach, the DOL frequently cites the lack of these documents or structures as probative of the fiduciary breach.

For that reason, although not necessarily required by law, it can be helpful for a plan to have in place these documents and structures such as an investment policy, a fiduciary committee, regular committee meetings, and well documented committee minutes.

On the other hand, to the extent a plan uses these documents, the DOL will often examine those materials carefully and treat them as definitive evidence of the plan's fiduciary actions. For example, the DOL routinely asks for and reviews all recent committee meeting minutes, and will often cite the statements in such minutes as irrefutable fact. For that reason, care should be taken to ensure that such fiduciary documents (and especially committee meeting minutes) are up to date and accurate, and do not misrepresent any facts.

Similarly, if the plan uses an investment policy statement, the DOL will often take the position that the policy is a "plan document" and that ERISA Section 404 requires the plan's fiduciaries to follow the terms of that investment policy. Although there is disagreement with this interpretation of the law, it is generally the position taken by the DOL. Accordingly, care should be taken to keep the investment policy statement up to date and follow any such policy when investing the plan's assets.

6) Fiduciary Duties and Prohibited Transactions

In general, the DOL has been consistently focused on enforcing ERISA's core fiduciary duties and

prohibited transaction rules. To that end, the DOL is always considering whether a plan has been involved in any breaches of fiduciary duty or prohibited transactions.

For example, the DOL often examines whether plan assets are being used to pay nonplan expenses, such as plan sponsor expenses, which can be a nonexempt prohibited transaction. One element of this is whether the plan can pay for the salaries of plan sponsor employees. DOL guidance permits such payments in certain circumstances (namely if the services would not have been incurred but for the plan). Where plan sponsor employees have a portion of their salaries paid out of the plan, the DOL will often examine those payments and evaluate whether they comply with that standard. A related issue is whether the plan has properly set up its program for reimbursing the sponsor for plan-related expenses. Among other things, such reimbursements should be made in accordance with a loan agreement in order to avoid a nonexempt prohibited transaction. More generally, the DOL is concerned with any type of loan from the plan that is improper. Finally, the DOL generally has a concern with unreasonable expenditure of plan expenses, such as using plan assets to pay for overly expensive conferences or other inappropriate benefits for plan fiduciaries. This is particularly a focus (and a subject of DOL scrutiny) for multiemployer plans that do not have a plan sponsor to pay expenses related to the plan.

7) Plan Investment Conflicts

A subset of the DOL's interest in ERISA's fiduciary duty standards is the agency's "Plan Investment Conflicts" national enforcement priority. The DOL describes this initiative as being focused on fiduciary service provider compensation and conflicts of interest, including fiduciary service providers and investment managers that have conflicts of interest that may lead to conflicted decisionmaking processes, imprudent application of investment guidelines, and payment of excessive fees. For example, the DOL is concerned with circumstances where a fiduciary advisor selects investment options on the basis of revenue sharing or fee sharing in a manner that is not properly disclosed to the plan or otherwise violates ERISA. With respect to plan administrators, the key inquiry by the DOL will be whether the plan's fiduciaries are adequately engaging in due diligence related to such plan investments and service providers in order to identify and address these types of conflicts of interest.

The initiative also examines improper or undisclosed compensation, such as undisclosed indirect compensation. In this regard, the enforcement initiative ties in with the DOL's participant (404a-5) and plan level service provider (408(b)(2)) disclosure requirements and the agency's focus on comprehensive disclosure about service provider compensation and conflicts of interest. For example, it is routine for the DOL to request a plan's 404a-5 disclosures sent to participants and 408(b)(2) disclosures received by service providers, and to cite any gaps in the delivery or receipt of those documents.

Finally, the "Plan Investment Conflicts" initiative includes criminal investigations of potential fraud, kickback, and embezzlement involving investment managers and advisers to plans and participants. Every year, the DOL assists in many criminal investigations and prosecutions involving these types of crimes.

8) Hard-To-Value Assets

In February 2012, the US Government Accountability Office (GAO) issued a report finding that the DOL has not taken sufficient actions to regulate retirement plan investments in hedge funds and private equity funds. The report also expressed concern with the DOL's limited focus on these investments, including investment losses and other challenges such as limited liquidity and transparency. Following the GAO report, in September 2013 the DOL Office of the Inspector General (OIG) issued a similar report focused on DOL regulation of ERISA plan investments in hard-to-value assets. In particular, the report concluded that the DOL had not taken sufficient steps to regulate plan holdings of "hard-to-value" assets and that "[a]s a result, plans are using poor practices in valuing these investments." Among other things, OIG recommended that the DOL improve enforcement in this area. After issuing its report, OIG sent a number of letters to retirement plans requesting information and documents on their valuations of hard-to-value assets. The letters also seem focused on whether the plan sponsor relies on the value provided by the fund manager or whether a third-party (such as the plan's trustee or another party) independently reviews that value.

Since the GAO and OIG reports, and the OIG requests, the DOL has shown some investigatory interest in hard-to-value assets, especially in defined benefit plans. For example, document requests of defined benefit plans often ask for "documents regarding the investment of the Plan in any alternative investments, including but not limited to mortgage backed securities, commercial paper, foreign obligations, and 'other' investments." There have also been requests for appraisals for plan investment options where "the market value . . . is not readily determinable" and information regarding off-shore investments.

Based on these requests, it seems clear that the DOL has some investigatory focus on hard-to-value assets, especially around defined benefit plans. However, thus far it does not appear that this interest has yet translated into a high quantity of investigatory findings of fiduciary breach or recoveries by the DOL. Nonetheless, plan investment fiduciaries should

take care to evaluate and monitor the plan's hard-to-value assets.

9) Proprietary Funds and Services

For those plan sponsors that offer services to retirement plans, or investment funds, the DOL has conducted a number of investigations on the use of those proprietary services or proprietary investment funds. This initiative is similar to (and raises similar issues to) the private plaintiff cases that have been brought in recent years regarding proprietary services and funds. The DOL appears to have conducted a number of investigations on this issue, and appears focused on whether the services and funds were selected and retained after an adequate fiduciary process (in addition to considering proprietary fund issues) and has made adverse findings in at least some of them.

One of these investigations recently ended in a significant judgment. In April 2019, the U.S. Court of Appeals for the Ninth Circuit upheld (in *Acosta v. City National Corporation*) a $7.4 million judgment that was based upon a finding of a 406(b) self-dealing prohibited transaction due to a bank using its own recordkeeping services for the retirement plan of its employees, and in so doing collecting compensation through revenue sharing.

In light of this initiative, plans that utilize proprietary funds or proprietary services consider a self-review of those investment options or services.

10) ESOPs

Employee Stock Ownership Plans (ESOPs) are defined contribution plans designed to invest primarily in the stock of the sponsoring employer. ESOPs can be standalone or components of a larger defined contribution plan.

The DOL has been very focused on investigating ESOPs since at least 2005, when it established the ESOP National Enforcement Project. In examining ESOPs, the DOL has been focused on such issues as whether the employer securities have been correctly valued (when purchased, sold, or distributed); the failure to provide participants with the specific benefits required or allowed under ESOPs, such as voting rights, participant distributions, and stock sale rights; and whether corporate governance is being passed on to participants correctly. These investigations make up a significant portion of DOL enforcement work and recoveries. For plans that are not standalone ESOPs, the DOL's focus is still of concern if the plans maintain an ESOP component.

Brian J. Dougherty, a partner at Morgan, Lewis & Bockius LLP and co-leader of the firm's Plan Sponsor Task Force, counsels and represents clients in a range of employee benefits and ERISA-related matters. Elizabeth S. Goldberg is an associate at the firm advising clients on ERISA matters with a focus on Department of Labor matters and investigations, fiduciary responsibility provisions, prohibited transaction rules and exemptions, and the management of employee benefit plan assets. The authors may be reached at *brian.dougherty@morganlewis.com* and *elizabeth.goldberg@morganlewis.com*, respectively.