

Business Owners May Be Liable for Employee 401(K) Investment Losses!

February 20, 2008 - U.S. Supreme Court unanimously ruled that an individual participant may bring suit for fiduciary breaches under the Employee Retirement Income Security Act (ERISA) to recover losses in an individual account.

Are you aware? A business owner may be liable to employees for their possible investment losses. You are a good business owner and installed a 401(K) plan to help your employees. But with so much to juggle and a business to run, did you miss the memos about how to run a 401(K) plan?

Owners hire a plan provider and employees enroll—then it is back to business as usual. Several years go by with very little attention to the 401(K) project until an ERISA complaint is filed with the US Department of Labor (DoL). Did you follow the rules of Section 404(c)?

Are you liable? “Why would I be liable? What did I miss? What is Section 404(c)? We have a 401(K) – that is as good as it gets.” Did your 401(K) process overlook the maintenance required by the DoL to protect the rights of the employees? Failure to completely deliver Section 404(c) compliance exposes the personal assets of the employer to each employee for investment losses they may experience. This risk is exacerbated by occasional stock market volatility. If you have a 401(K) you should investigate why this is so important.

Let’s look at an example: Assume you decide to provide a lunch facility in your business to help employees. You pay caterer, review the initial menu, have the employees pay a nominal charge to cover the cost of food. Most employees use the facility and are appreciative of your effort. Several years later James age 51 dies of heart

complications. Within a few weeks you are served as the defendant in a “wrongful death” lawsuit alleging – you set up the food service, you hired the caterer, you selected the menu – thus James had to eat what was served or go hungry. His heart complications were compounded by the lack of “healthy choices”, too many saturated fats, high cholesterol and the absence of information about the nutritional content of the food being served. The court orders you to pay Mrs. James \$1,000,000 in damages – your liability insurance does not cover food service. The court reasons, you should have obtained the services of an independent food service consultant to oversee and monitor the nutritional value of the food “on the menu”.

In this lunchroom example, your employees can only eat items “on the menu”. A retirement plan works the same way. Employees can only select 401(K) investments from a list that is created and maintained by the employer.

If the menu is not up to par, it’s not a matter of: Will you have a DoL complaint, but when will you have a DoL complaint. The U.S. Supreme Court has empowered the layperson in our litigious society to take action against business owner for “serving the wrong 401(K) menu”.

See - *LaRue v. DeWolff, Boberg & Associates, Inc.* (No. 06-868, Feb. 20, 2008) *the U.S. Supreme Court.*

What can be done to Protect the business owner from this liability?

Become Aware of 404 (c). *Caveat (Latin, Let him beware.)* Seek to remove the DoL complaint by using the protection afforded the employer as set forth in ERISA 404(c). Section 404(c) provides a process designed to empower the employees with information and protect the employers who make the effort to provide the plan information to the employees. [A bulletin issued by the Department of Labor \(96-1\) clarifies what this means – see below.](#)

What 404c Requires

Some fiduciaries have skimmed summaries of 404c and concluded that they are "safe" if the plan offers participants at least three diversified investment choices, along with opportunity to make frequent changes among them. However, the regulation clearly specifies that participants also must have "sufficient information to make informed investment choices." A subsequent Interpretative Bulletin issued by the Department of Labor (96-1) clarifies what this means, as well as the potential loss of 404c protection for companies that offer participant investment advice.

Forget the lunch room! Have you managed your employee's 401(K) issues like the lunch room example? Do your employees have informed choices? Apply the same process and expect the same result. You have the choice, a) keep the same process, or b) bring in a consultant to review your 401(K) compliance.

We can assist by evaluating your risk and help you get in front of possible problems. We are not just another 401(K) salesman, but we are part of a team of experts in Texas skilled in analyzing these issues. We are not asking you to write a check or change your plan – just evaluate your plan's compliance.

If there is nothing wrong with your plan, you will have our written report to document you have reviewed your compliance with the law. Use our report to fend-off the calls from the numerous 401(K) salesmen.

Jack Dyer and Denver Dyer are registered representatives of and offer investment advisory services through LaSalle St. Securities, LLC and La Salle St. Investment Advisory respectively. LaSalle St. Securities, LLC is a registered broker/dealer and member FINRA/SIPC. LaSalle St. Investment Advisory is a federally Registered Investment Advisor located 940 N. Industrial Dr., Elmhurst, IL 60126 Jack Dyer and Denver Dyer are located in the Tyler, Texas Branch office 903 509-2289 at 3304 S. Broadway, Ste 101, Tyler, Texas 75701 www.income-portfolio.com

Here is a 404c compliance checklist:

1. Have all eligible participants been clearly informed that the plan intends to comply with 404c?
2. Have participants been given the name, address and phone number of the plan fiduciaries responsible for providing investment information?
3. Does the plan have a written Investment Policy Statement (IPS) and does it explicitly state that the plan intends to comply with 404c?
4. Has the plan's annual Summary Plan Description been checked against specific requirements of 404c? Has this process been documented in the plan's compliance file? Have plan documents been reviewed by an ERISA compliance attorney?
5. Does the plan have a published schedule of participant information and education events? Is a document file maintained, containing copies of all communications with plan participants? At every meeting with plan participants, is a list of attendees recorded and filed?
6. Have any restrictions on transferring to or from an investment choice been clearly communicated to participants?
7. Have all transaction fees and commissions that affect the participant been disclosed? Specifically, have participants been given a description of the annual operating expenses of each designated investment alternative?
8. The DOL has defined four specific categories of participant communication that do not constitute "investment advice" for purposes of limiting 404c protection. They are:
 - 1) plan information
 - 2) general financial and investment information
 - 3) asset allocation models
 - 4) interactive investment materials, such as worksheets, PC illustrations, etc. The common denominator of all four is that they don't steer the participant in any particular investment direction. Does the plan's investment advice meet this test?
9. If an asset allocation model identifies a specific investment alternative available under the plan, have participants been advised that investment alternatives with similar risk and return characteristics also are available?
10. If calculators are used in investor education, are they based on generally accepted investment theories? Do they clearly disclose the "what if" assumptions on which they are based, such as retirement age, income levels, inflation rates, rates of return, and all plan investment alternatives?
11. Has the plan taken a survey of participants to determine their level of investment knowledge? Are plan communications written in a style and language that participants can clearly understand?
12. Are plan fiduciaries aware of specific duties that may not be delegated or protected under 404c, including prudent selection and monitoring of investment menu choices?
13. Does the plan have a formal process for evaluating investment managers' adherence to fund objectives, including a written evaluation report?
14. Does the plan have fiduciary liability insurance from a carrier such as American International Group (AIG); Lloyd's of London, Reliance Insurance, Travelers Property Casualty, or Chubb Executive Risk? The cost of this coverage typically is about 5% of the coverage limit purchased -\$25,000 per year for a \$5 million policy. Premiums can double or triple for participant-directed plans that offer either of two investment choices:
 - 1) company stock
 - 2) a self-directed brokerage option.

The 404c regulation is published by the DOL here:

http://www.dol.gov/dol/allcfr/ebsa/Title_29/Part_2550/29CFR2550.404c-1.htm

LaRue v. DeWolff, Boberg & Associates, Inc. (No. 06-868, Feb. 20, 2008) the U.S. Supreme Court – “In a decision that has significant implications for employers that sponsor 401(K) and other defined contribution plans, the U.S. Supreme Court unanimously ruled that an individual participant may bring suit for fiduciary breaches under the Employee Retirement Income Security Act (ERISA) to recover losses in an individual account.”