AIG Retirement

403(b) Plan Update:

Do public schools have a *fiduciary duty* to review the investment products available under their 403(b) plans? *The answer may surprise you.*

Plan sponsors may have many reasons for wanting to review their investment products, in addition to confirming that the products and providers satisfy applicable provisions of the final 403(b) regulations. The question this article addresses is: *is the potential for fiduciary liability one of those reasons?*

The looming deadline for implementing the requirements of those final regulations (generally, January 1, 2009, subject to certain delayed effective dates) can pose both challenges and opportunities for employers considering an investment product review at the same time it is making compliance decisions regarding the new requirements under the regulations. This makes it all the more important for plan sponsors to sort out the correct information from the incorrect information. That task can be difficult, however, and in some cases may not occur until decisions have already been made and action already taken: in other words, when it may be too late. The purpose of this article is to help shed some light on the question, not by providing legal or tax advice (it does not), but by providing important relevant information to assist in the employer's discussion with their counsel.

Summary of Conclusions:
Any response to this question will require state-specific analysis. One point that becomes quite clear, however, is that any party asserting that such liability already exists may have a very difficult task demonstrating the assertion to be true, in a number of states. If there is a source of fiduciary liability for these public employer plans:

- it is not found in Section 403(b) of the Internal Revenue Code or in the recently issued regulations thereunder. Even though the final regulations continue a trend that began in 1986, to add new requirements to what started out as a very simple account-based plan, the regulations do not (nor could they) add a new layer of fiduciary duties on top of what are very clearly compliance duties. And,
- it is not found in Title I of ERISA. Even though Title I of ERISA does impose fiduciary duties, it and those duties are inapplicable to public employers. In light of that broad exemption, existing or future litigation interpreting the rules and exceptions under ERISA are also inapplicable to such public employers.[1]

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[1] For example, a recent decision of the United States Supreme Court addressed what claims a participant might assert against a plan fiduciary for a failure to properly process a requested transaction, under an ERISA plan. LaRue v. DeWolff, Boberg & Assoc., 128 S. Ct. 1020 (U.S. 2008). Because the decision only interpreted the provisions of ERISA, it would not be applicable to a non-ERISA plan sponsored by a public employer. However, it should also be noted that the types of individual annuity contracts and custodial accounts frequently offered in public employer 403(b) plans, as well as in many allocated group annuity and custodial arrangements, already afford a participant a contractual right, as well as a right under applicable securities laws, to obtain correction of a recordkeeper's error in processing an otherwise properly requested transaction. Thus, in that sense the recent decision by the Supreme Court might be viewed as affording to ERISA plan participants rights that many 403(b) participants already enjoyed. However, participants in unallocated arrangements in non-ERISA plans (including public 403(b) plans) may not enjoy similar rights.

That leaves state law, which can appear in several forms. Some state 403(b) enabling statutes (and/or interpretations by the state's attorney general) specifically limit or eliminate entirely a plan sponsor's potential liabilities under these plans, while many others are simply silent as to any such liabilities, neither imposing them nor necessarily ruling them out. This leaves a future plaintiff in many cases searching for an argument under laws governing state retirement systems, which frequently will not apply to these plans, or under a state's version of such laws as the Uniform Prudent Investor Act or the Uniform Fiduciaries Act, or related state trust laws, which are likely to be inapplicable unless the plan sponsor is determined to be a fiduciary

- *for this particular function*
- without regard to those statutes.

Even if a public employer might be considered to have a fiduciary role with respect to its employees for certain purposes[2], the question here is whether they are a fiduciary with respect to the plan generally and with respect to identifying available investment products specifically.

Does this mean that a public employer plan sponsor that does not have a fiduciary duty to evaluate plan investment products may not do so, or that even if such a review is permitted the employer should avoid it? No, it does not mean either of those things. What it does mean is that plan sponsors should make their decisions based on the duties that actually apply, and based on their own goals and objectives with respect to the plan.

Why should employers care whether they are fiduciaries?

The fiduciary question is an important one, because the answer can go a long way toward helping plan sponsors determine both:

- what their duties are, and
- what standards apply to those duties.

TRUE OR FALSE: The new plan document requirement in the regulations makes a public school plan sponsor a fiduciary.

False. The new plan document requires the employer to recognize its ownership and control of the plan, by formalizing the plan into a document or collection of documents.

2 There are some court decisions that have found a public school to be a fiduciary with respect to its employees. See Davis v. Greenwood School District 50, 620 S.E. 2d 65 (S.C. 2005). Davis is a South Carolina Supreme Court decision that interprets and applies South Carolina law. The decision also appears to narrowly apply the fiduciary status to specific duties that the district has to the employee, in this case with respect to a duty to pay a promised incentive for teachers to obtain certain certifications.

Stated another way, *what is their potential liability if they don't get it right*? This is not an insignificant question. While some might urge public plan sponsors to undertake fiduciary duties even if they do not technically apply, many legal advisors to those sponsors, if asked, would offer a very different recommendation. Fiduciary duties, as a general matter, are higher duties which can carry correspondingly higher levels of potential liability. The following excerpt from Black's Law Dictionary can provide a starting point for understanding what this can mean in the context of a fiduciary relationship:

> Fiduciary relationships — such as trustee-beneficiary, guardian-ward, agent-principal, and attorney-client — require *the highest duty of care*. Fiduciary relationships usually arise in one of four situations: (1) when one person places trust in the faithful integrity of another, who as a result gains superiority or influence over the first, (2) when one person assumes control and responsibility over another, (3) when one person has a duty to act for or give advice to another on matters falling within the scope of the relationship, or (4) when there is a specific relationship that has traditionally been recognized as involving fiduciary duties, as with a lawyer and a client or a stockbroker and a customer.[3] (*emphasis added*)

A fiduciary role may go beyond commonly understood concepts such as avoiding self-dealing or conflicts of interest, and could impose additional affirmative obligations, as well as potential corresponding legal liabilities. Simply assuming such duties can result in unintended consequences, including potential liabilities that are not covered in the employer's budget.[4]

TRUE OR FALSE: A 403(b) plan sponsor now must personally approve all distributions and transfers.

False. Taking control of, and recognizing responsibility for, the plan does not mean the employer has to approve distributions and transfers. It does mean that the employer needs to make conscious decisions about who will perform those functions, and structure arrangements accordingly.

The alert reader might ask whether someone who seeks to avoid application of fiduciary duties is running away or has something to hide. However, a plan sponsor's counsel will likely have a different view, and very different advice. They might remind the plan sponsor, for example, that they routinely seek to limit their potential liabilities in contracts, relationships, and daily decisions. They might also point out that it is not about avoiding doing the right things. Instead it is about doing the right things for the right reasons.

A conversation with the plan sponsor's counsel may also raise another important related point that can be too frequently overlooked: if fiduciary status applies, then unless it arises because of a recent change in statutes or regulations, or from a recent court decision, it is not new. This fact can be another very good reason for a plan sponsor to not simply assume that it is a fiduciary, without asking its counsel to do the necessary homework to determine whether this is actually true, since premature decisions on this front might have backward-looking consequences. Moreover, such consequences may not be limited to the 403(b) plan: what about selections the employer has made with respect to life, disability, and health benefits, as well as decisions on a number of additional fronts that could be affected by a sweeping conclusion of fiduciary status?

These are all questions which come into much sharper focus when the confusion regarding any direct ties between this issue and the final 403(b) regulations is resolved.

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3 BLACK'S LAW DICTIONARY (8th ed., p. 153).

4 Depending upon applicable state law, an employer also might find some protection under the state's sovereign immunity principles. Otherwise, it also should be noted that such matters may or may not be covered by the employer's insurance coverage.

Are these duties found in the 403(b) regulations? No.

Although attention to this question is coinciding with efforts by employers to implement the requirements of the final 403(b) regulations, it is important to make one point very clearly: for a public employer, *the question of fiduciary duty has no direct relationship to those regulations*. The word "fiduciary" occurs nowhere in the final regulations, or in the preamble to the regulations.[5] Moreover, any indirect relationship, *if it exists*, in some instances could be a result of the employer's decisions in response to the regulations, and not a necessary impetus to those decisions. Specifically, in some cases, while a plan sponsor may be under the impression that it needs to take certain actions because it is a fiduciary, in reality *it may be those very actions which are at greatest risk of making that plan sponsor a fiduciary*.

The final 403(b) regulations do require employers to take more responsibility for, and control of, their plans, both in plan design and in ensuring that appropriate compliance requirements are satisfied. The regulations are generally silent, however, as to how the employer should accomplish that compliance. While discussions of possible fiduciary duties often focus on the selection of permitted investment products for the plan, the truth is that apart from closing the door to new life insurance policies in these plans, the final 403(b) regulations do not prescribe any rules for selecting investment products in these plans, *though they have much to say about the compliance requirements for any such products*.

Are they found in Title I of ERISA? Not for public employers.

Related to the question of whether the final 403(b) regulations are the cause of this potential fiduciary status is the additional fact that another source of possible fiduciary status, Title I of ERISA, is plainly inapplicable to plans sponsored by public employers, as are the fiduciary requirements that ERISA would impose on a plan sponsor. Specifically, a governmental plan is excluded from the coverage of Title I of ERISA.[6] The IRS, in a Question and Answer section on its Web site regarding the final 403(b) regulations, also confirms this:

> Let us begin answering this question by stating right up front, particularly where education is concerned, to realize that any form of government is not subject to ERISA. So if we have a 403(b) in a public K-12 school, no matter what they did under that plan, it would not subject them to ERISA. Public universities are also not subject to ERISA.[7]

TRUE OR FALSE: The regulations require a public school to file its 403(b) plan document with the IRS for approval.

False. No plan sponsor is required to file their plan documents with the IRS for approval. However, IRS approval can provide confidence that the plan satisfies the first half of the "form and operation" requirement. The good news: public school use of IRS model language, either in its original form or as adapted to the employer's specific needs and objectives, can contribute significantly to that same employer's confidence level.

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5 26 U.S.C. § 403(b) (2007).

6 29 U.S.C. § 1003(b)(1) (2007); ERISA defines a "governmental plan" as "a plan established or maintained for its employees by the Government of the United States, by the government of any State or political subdivision thereof, or by any agency or instrumentality of any of the foregoing. The term "governmental plan" also includes any plan to which the Railroad Retirement Act of 1935 or 1937 applies, and which is financed by contributions required under that Act and any plan of an international organization which is exempt from taxation under the provisions of the International Organizations and Immunities Act (59 Stat. 669)." 29 U.S.C. § 1002(32) (2007).

7 Bob Architect, IRC 403(b) Tax-Sheltered Annuity Plans - Ask Bob Architect (2008), http://www.irs.gov/retirement/article/0,,id=172433,00.html (last visited May 8, 2008).

Are they found in the Investment Adviser's Act? Again, not for most public employers.

Before moving on to where the real analysis on this question lies, let's address one additional source of possible fiduciary liability for these public employer 403(b) plans, on the federal level. It is true that fiduciary duties generally will apply to an investment adviser, under The Investment Advisers Act of 1940, as amended (the "Adviser's Act").[8] The Adviser's Act defines an investment adviser as "a person who, for compensation, engages in the business of advising others."[9] An investment adviser normally will not give advice or make recommendations to a client without an oral or written investment advisory agreement setting forth the terms and conditions for the provisions of investment advice and the compensation for such advice. Further, the investment advisory agreement generally provides protection for the client, identifying that the firm has fiduciary responsibility to its client for the investment advice and recommendation.

Assuming that the plan sponsor is not making investment recommendations to plan participants for compensation, those fiduciary duties generally do not apply to a plan sponsor.[10] It would therefore be incorrect, absent direct or indirect action by the employer to render such advice for compensation, to describe these requirements as applying to a public employer sponsoring a 403(b) plan. Moreover, many employers will try very hard to avoid even appearing to fall under the investment adviser definition, and for very good reasons, since any employer actually making individual investment recommendations to plan participants, about where to invest their 403(b) accounts, may not only take on such duties and corresponding liabilities, but may be doing so without proper licensing.[11]

In 403(b) plans sponsored by public employers, an investment adviser might be engaged by:

- the employer, such as to assist in selecting either investment providers or individual investment options;
- the participant, either to make recommendations or to manage the participant's account; or,
- a provider, to advise regarding the selection of investment options within the provider's product and service offering.

If the employer has engaged the investment adviser, whether the employer assumes additional liability, and the scope or extent of any such liability, will likely be determined with reference to the source of the employer's general duties with respect to the plan. If either the participant or the provider has engaged the investment adviser, then it is likely that the employer could have no liability for the selection of the adviser or the advice provided by the adviser, assuming that the employer had no involvement and that the source of the employer's duties does not provide otherwise.

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8 15 U.S.C. §§ 80 b-1 et.seq. (2007).

9 15 U.S.C. § 80(b)-2(a)(11) (2007). The Adviser's Act also contains certain limited exemptions. Under an interpretation from the United States Securities and Exchange Commission, compensation can be either direct or indirect. Release No. IA -1092, S. E. C. Docket 494, 1987 WL 112702.

10 This point is independent of whether fiduciary duties might arise from another source.

11 The Securities Act of 1933 exempts certain securities and transactions from registration with the Securities and Exchange Commission, as does The Investment Company Act of 1940. The Adviser's Act, however, does not state exemptions for public or private employers who may take on advisory duties.

Then do such duties apply at all? Maybe.

Taken together, the fact that ERISA, the Code, and the Advisers Act do not directly impose these theorized fiduciary duties on 403(b) plans sponsored by public employers, leads to one important initial conclusion: *there is no basis for a blanket statement that all 403(b) plans maintained by public employers are now subject to fiduciary duties*. If there are any such duties, they must be found elsewhere.

All of this so far is good news for public employer plan sponsors. In general, both in-house and outside counsel to public employers sponsoring 403(b) plans maintain significant depths of expertise in many areas, however those may not include tax and ERISA matters. As a result, these employers and their counsel may instead be inclined to depend upon others, including counsel with more extensive 403(b) experience, as well as consultants, administrators, and investment providers. So why is it good news that the fiduciary question is not a tax or ERISA question? *Because it:*

- *takes the question out of what may be a mysterious realm for many practitioners whose expertise resides outside of the benefits world, and*
- *makes it a question of state laws and regulations, and applicable case law, very familiar areas to those legal advisors who are so integrated into the daily activities of these public employers.*

The bottom line: this is an issue that employers should approach with good information and good counsel. It is not enough to say, for example, that someone might file a suit, or point to other plan-related litigation.[12] An employer's counsel is trained to ask, with regard to any such potential litigation: what is the legal theory, and does that legal theory have merit? And it is also not enough to say that an employer could just accept the role of fiduciary even if it is not legally required: while the statement might be factually true, assuming no legal authority preventing such assumption, that conclusion by itself does not begin to address the advisability of such a status.

Going to the source: State law

Now that we know where these fiduciary duties *do not* originate for public plan sponsors, what might be some of the possible sources of these duties, if they apply?

To start with, we should return to an earlier process point. How can a public education employer determine whether fiduciary duties apply to their plan? The short answer is that employers should consult with their counsel on these and all significant benefit plan matters. The remainder of this article will explore some of the places that counsel may look for answers to the question.

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12 Litigation with respect to retirement plans generally is not unusual. However, it is also important for an employer and its counsel to pay attention to specific details, such as the:
- Status of the litigation: Is it decided or in progress?
- Application of any precedent: Is it authoritative for my state, my organization?
- Relevance of the decision: As noted regarding the recent decision of the U.S. Supreme Court in LaRue, a decision regarding the interpretation of LaRue does not directly affect a public employer's non-ERISA plan. Similarly, the existence of a lawsuit alleging misconduct by a private organization over its role with respect to one or more types of plans may not even begin to answer questions about the employer's own duties under the plan.

State enabling statutes

Since so much of what public employers may do is both prescribed and circumscribed by state statutes and regulations, perhaps the most obvious place to start is in any state statutes directly applicable to the public employer's 403(b) plan. These might include general authorizing language, for the plan or for the salary reductions, and they may also include additional statutory provisions. Some of these statutes may explicitly impose fiduciary duties, while others take the opposite approach and strictly circumscribe the employer's responsibilities, and still others are entirely silent on the issue. The following reflects a sampling of the variety of such statutes:[13]

Imposing fiduciary duties

One example of a state statute expressly imposing a fiduciary standard with respect to a 403(b) plan applies to a narrow set of plan sponsors in Minnesota. It applies specifically to teachers retirement fund associations in the cities of Duluth and St. Paul, Minnesota, and appears to impose fiduciary duties with respect to the plans that the associations are authorized to establish, including the 403(b) plan.[14]

TRUE OR FALSE: All investment products in a 403(b) plan must have identical provisions.

False. This is not even true for qualified ERISA plans, much less for public school 403(b) plans. Of course, different provisions across available products – such as loan availability and distribution options – must comply with the requirements of the Code and regulations as well as being consistent with the terms of the plan.

Expressly limiting the employer's duties

In stark contrast to that Minnesota statute, a number of states have written into their statutes express limitations on the liability of the employer with respect to the program. It is likely that the focus of such limitations is on claims by participants, since as a general matter state statutes could not preempt federal tax consequences to the employer from these plans.

The following examples (this is not an exhaustive list, nor does it represent exhaustive state-by-state research) provide a sampling of the types of express limitations that can be found in some of the other state statutes governing public school 403(b) programs:

> **Minnesota**: Minnesota itself has taken a more restrictive approach in some other statutes governing the supplemental plans for school districts or other governmental subdivisions or state agencies, imposing liability *limitations*. One statute authorizes the State Board of Investment (SBI), upon request of a provider
>
> > …to review the financial standing of the company, the competitiveness of its investment options and returns, and the level of all charges and fees impacting those returns.[15]

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13 There is another reason for emphasizing that this is only a sampling. A protective provision of one statute may be overridden by a provision of another statute, or interpreted differently by a court or a qualified state official, such as a state's attorney general.

14 MINN. STAT. § 354A.021 (2007)

15 MINN. STAT. § 356.24 (2007).

That same section expressly prohibits the SBI from being considered a fiduciary in providing such review. In another statute governing powers of independent school districts, a provision authorizing 403(b) contributions also provides that a separate statute governing employment, contracts and employee termination, Section 122A.40

> shall not be applicable hereto and the board shall have no liability thereunder because of its purchase of any individual annuity contracts.[16]

Yet another statute specifically authorizes the establishment of 403(b)(7) custodial accounts and provides some detailed direction as to the type of investments and the levels of fees, but is silent as to fiduciary or related liabilities.[17]

Alabama: A statute seems to place very clear limitations on the employer's potential liability with respect to its 403(b) program:

> When amounts have been correctly deducted and remitted by the board or postsecondary institution, the board or secondary institution shall bear no further responsibility or liability for subsequent transactions. No board or post-secondary institution shall be liable for any error when acting in good faith pursuant to this section.[18]

Arizona: A statute authorizing school districts, community colleges and universities to establish several types of plans, including 403(b) plans, provides that

> The amount to be invested shall be determined by the employee not less than fifteen days before the employee's first payday in the school year, or any time during the school year at the option of the governing body. The employing body or county school superintendent shall assume no responsibility other than to make the requested payments during the actual time of the employment of the employee.[19]

Washington, Iowa and Massachusetts: A Washington statute authorizing the establishment of 403(b) programs for public schools permits employees to select any provider for their 403(b) investment as long as that provider has signed up at least five employees, and otherwise provides that those organizations shall not restrict

> …employees' right to select the tax deferred annuity of their choice or the agent, broker, or company licensed by the state of Washington through which the tax deferred annuity is placed or purchased…[20]

Iowa and Massachusetts appear to have similar rules.[21]

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16 MINN. STAT. §123B.02 (2007).

17 MINN. STAT. §356.24 (2007).

18 ALA. CODE 16-22-6 (2008).

19 ARIZ. REV. STAT. § 15-121 (2008)

20 WASH. REV. CODE ANN. § 28A.400.250 (2008).

21 IOWA CODE § 294.16 (2008); MASS. GEN. LAWS ch. 71, § (2007) .

Texas, California: Both of these states impose restrictions similar to those in Washington, Iowa and Massachusetts, on the employer's authority to exclude products and providers under the 403(b) plan. They both also limit employee selection to the providers and products listed on registries maintained by the state's retirement system. In addition, Texas permits employers to exclude providers, but only to the extent necessary to comply with 403(b) requirements.[22]

Ohio: Like Texas, California, Washington, Iowa and Massachusetts, Ohio imposes significant limitations upon a school district's ability to restrict providers under the 403(b) plan, and further requires that:

> (A) The designee must execute a reasonable agreement protecting the institution or district from any liability attendant to procuring the annuity;[23]

West Virginia: A statute authorizing the establishment of 403(b) programs for teachers and other employers specifically provides that

> The purchase of such tax deferred investment for a teacher or other employee by a board of education, the teachers retirement board, the West Virginia Board of Education and the board of regents [abolished] of West Virginia and their agencies shall impose no liability nor responsibility whatsoever on said boards or members thereof except to show that the payments have been remitted for the purposes for which deducted.[24]

Florida: A statute authorizing the establishment of tax-sheltered annuities or custodial accounts for employees of government agencies incorporates a provision which is nearly identical to the West Virginia provision:

> The purchase of such tax-sheltered annuity or other investment qualified under the United States Internal Revenue Code and not prohibited under the laws of this state for an employee shall impose no liability or responsibility whatsoever on the employing agency except to show that the payments have been remitted for the purposes for which deducted.[25]

Michigan: A Michigan statute clearly describes a school district's limited liabilities for the 403(b) plan:

> (2) The board shall not have liability because of its purchase of tax-deferred investments for employees.[26]

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22 TEX. REV. CIV. STAT. art. 622a-5 (2007); Cal. Educ. Code §§ 24950 – 24953; 25100 – 25115 (2007) .

23 OHIO REV. CODE § 9.91 (2008).

24 W. Va. Code § 18A-4-12 (2007).

25 Fla. Stat. ch. 112.21 (2008).

26 Mich. Comp. Laws § 380.1224 (2008).

Tennessee: A Tennessee statute authorizing school districts to establish and maintain 403(b) programs imposes an affirmative duty on the district to review the investment providers, but only with respect to the selection of one or more providers to receive an optional employer matching contribution, and not with respect to an employee's optional deferrals. The statute does not specifically mention fiduciary duties, but does prescribe some of the important selection requirements, including minimum ratings for insurance company providers, as well as maximum fee levels for annuity products. The statute also imposes an obligation to ensure that all contracts, regardless of contribution source (employer, employee) satisfy applicable 403(b) requirements:

> Any annuity or other contract entered into under the authority of this section shall conform to all applicable laws, rules and regulations of the internal revenue service which will qualify such contracts for income tax benefits provided for under the Internal Revenue Code of 1986, § **403(b)**, or any subsequent corresponding Internal Revenue Code of the United States, as from time to time amended. [27]

Maine: A Maine statute also appears to impose limitations on a school district's potential liabilities under the 403(b) plan, describing an intent that districts be able to provide the programs:

> …without loss to themselves, or to the school administrative unit, school, educational institution, or Department of Education to which they belong, of any benefits, subsidies, or opportunities therefore that they might otherwise be entitled to under the laws of the State of Maine.[28]

Nevada: A Nevada statute may be even more limiting. A condition for offering the 403(b) program is:

> 2. That purchase must be made only upon the written request of the employee and upon agreement in writing that:
> …
> (c) The board of trustees has no liability under any such arrangement.[29]

Indiana: An Indiana statute, as interpreted by an opinion of the state's attorney general, appears to require a school district to send contributions to any annuity provider that has signed up at least 20% of the district's teachers, and the requirement may also apply to non-teaching employees:

> It is my official position that public school teachers are entitled to designate the recipients of funds withheld for insurance or annuity purposes from their salaries if 20% or more of the teachers of a school corporation designate the same recipient. It would be reasonable to follow the analogy of the provisions concerning teachers and hold that non-teaching employees of school corporations have the same right as teachers to designate the recipient of funds withheld from their salaries.[30]

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27 Tenn. Code Ann. § 49-2-208 (2008).

28 Me. Rev. Stat. tit. 24 § 4502 (2007).

29 Nev. Rev. Stat. § 391.380 (2007).

30 Ind. Code § 20-28-2-22 (2007); Ind. Att'y. Gen. Op. 29, Nov. 24, 1971.

Missouri: A Missouri statute includes relief for certain good faith errors:

> A board of education when deducting amounts from the compensation of employees as directed by the employee shall not be liable for any good faith error.[31]

New York: An opinion of the New York Attorney General provides an illuminating discussion of the potential liabilities of New York public schools sponsoring 403(b) plans:

> A more difficult question is whether a school district may be liable to an employee even though the district fully performs its basic contractual obligations. For instance, may a school district be liable if an annuity or custodial account is not granted the expected tax advantages or if the company selling an annuity or custodial account does not fulfill its obligations?
>
> It seems that a school district should not be held accountable for the soundness of a particular company's annuity plan or performance. That is a matter between an individual employee and an individual company. An employee is free to choose a particular company after comparing different plans. A school district is merely an agent of its employee in deducting money from his/her paycheck and forwarding it to the chosen company. A school district does not have a duty to supervise the manner in which individual plans are administered (see Van Ostrand v. National Life Assurance Co. of Canada, supra). Of course, to the extent that a school district makes representations concerning the relative merits of different plans, it may be risking greater responsibility to its employees. The safest course for a school district is to let the employees themselves or their union evaluate and compare competing plans.
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> The State Department of Education recommends (and we concur) that a school district take steps to protect itself, including the following: insertion of language in the agreement with the employees (probably the payroll deduction authorization) limiting the school district's role in the transaction, and stating that the employee agrees not to seek recovery from the district for loss which might be suffered because of the acts or omissions of the company selling the plan, or acts or omissions of the disbursing company when one of several companies acts as disbursing agent for the school district in forwarding payroll deductions to individual accounts with the several companies (see Opns St Comp, 1980, No. 80-121); and, insertion of language in the agreement with the disbursing company (when one exists) whereby that company will hold the district harmless from financial loss which might result from the disbursing company's acts or omissions.[32]

Kentucky: A Kentucky statute also describes a limitation of liability for a school district sponsoring a 403(b) plan:

> (c) Health insurance, life insurance, and tax-sheltered annuities shall be interpreted as separate types of deductions. When amounts have been correctly deducted and remitted by the board, the board shall bear no further responsibility or liability for subsequent transaction.[33]

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31 Mo. Rev. Stat. §168.300 (2008).

32 N.Y. Att'y. Gen. Op. No. 81-394.

33 Ky. Rev. Stat. § 161.158 (2008). In addition, in a 1974 opinion, the Kentucky Attorney General determined that a provision in a proposed agreement relating to a 403(b) program that imposed liability for negligence upon a county school system was improper under this section and under the doctrine of sovereign immunity. Ky. Att'y. Gen. Op. 74-414.

No clear references regarding liability

A number of state 403(b) enabling statutes appear to be silent as to any level of liability, fiduciary or otherwise. A few examples of such statutes include: Nebraska;[34] North Carolina;[35] Georgia;[36] Hawaii;[37] Illinois;[38] Indiana;[39] Kansas;[40] Louisiana;[41] Maryland;[42] North Dakota;[43] Oklahoma;[44] Oregon;[45] Pennsylvania;[46] South Carolina;[47] South Dakota;[48] and, Wyoming.[49]

Once again, this is a sampling and not an exhaustive 50-state review and analysis. However, it underscores the importance of reviewing the actual statutes before concluding either for or against fiduciary status.

What does it all mean? What probably stands out most from these examples is that, in many states, the potential for employer liability under these plans was consciously considered and addressed, likely with an eye toward potential claims from employees. That does not guarantee that another statute might not reduce or modify those protections, or that a state's legislature will not modify these provisions in the future.[50] It also does not support a broad conclusion that employers in other states also do not have such liabilities. However, if nothing else, it clearly indicates that no blanket statement about fiduciary liability could possibly be accurate.

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34 Neb. Rev. Stat. Ann. § 79-514 (2007).

35 N.C. Gen. Stat. § 115C-341 (2007).

36 Ga. Code § 47-3-1 (2007).

37 Haw. Rev. Stat. § 303-2 (2007).

38 105 Ill. Comp. Stat. 5/10-22.3a (2008).

39 Ind. Code § 5-10-1.1-1.

40 Kan. Stat. .Ann. § 72-8603 (2006).

41 La. Rev. Stat. § 17: 1315 (2008).

42 Md. Code Ann. State Pers. & Pens. § 35-404 (2008).

43 N.D. Cent. Code § 54-44-04.1 (2008).

44 70 Okla. Stat. Ann. tit. 70, § 6-101.1 (2007).

45 Or. Rev. Stat. § 243.820 (2007).

46 24 Pa. Cons. Stat. § 11-1142 (2007).

47 S.C. Code Ann. § 9-15-10 (2007).

48 S.D. Codified Laws § 3-10-4 (2008).

49 Wyo. Stat. Ann. § 9-3-508 (2007).

50 This paper has not analyzed the possible availability of sovereign immunity provisions of a state's law, either in addition to or in lieu of the statutes discussed in this paper. In addition, with respect to potential changes in a state's laws, it is certainly possible that a failure to understand existing protections in a state's laws could result in support for legislation to "limit" nonexistent fiduciary duties and liabilities for public 403(b) plan sponsors, and result in the actual creation of such explicit statutory duties.

State pension system statutes; other state fiduciary statutes

Another source of potential fiduciary duties may come from state pension statutes. Similar to the above discussion, each of these would need to be evaluated individually by plan sponsors and their counsel. It is quite common for such statutes to impose fiduciary duties; however, such duties generally apply to the board maintaining the plan and generally with respect to the investment of funds specifically supporting the defined benefit pension obligations of the state. For example, the governing board for California's Public Employees' Retirement System is required to

> …discharge their duties with respect to this system solely in the interest of the participants and beneficiaries:
> (a) For the exclusive purpose of both of the following:
> (1) Providing benefits to members, retired members, and their survivors and beneficiaries.
> (2) Defraying reasonable expenses of administering this system.
> (b) Minimizing the employers' costs of providing benefits under this part.
> (c) By investing with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with those matters would use in the conduct of an enterprise of a like character and with like aims. [51]

However, unless such statutes also govern an individual employer's 403(b) plan, or unless the 403(b) plan itself is maintained at the state level, it is unlikely that the fiduciary provisions applicable to the state pension plans would extend to such 403(b) plans.

Last but not least, another potential source of fiduciary duties that is sometimes mentioned in conjunction with public employer 403(b) plans is one of two documents – a Uniform Fiduciaries Act[52] or a Uniform Prudent Investor Act.[53] Many states have adopted versions of one or both of these acts, or may have included similar provisions in state trust law. These statutes generally do not impose fiduciary status on a party, but instead set forth duties and standards for individuals who are trustees or are otherwise determined to be fiduciaries.[54] A prefatory comment to the Uniform Fiduciaries Act makes this point very clearly:

> The Act covers situations which arise where one person deals with another person whom he knows to be a fiduciary. Questions relating to actual or constructive notice of the existence of a trust or other fiduciary obligation are not within the scope of the Act; it deals with questions relating to notice of the breach of a fiduciary obligation.[55]

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51 Cal. Gov't. Code § 20151 (2007).

52 Unif. Fiduciaries Act (1922) §§ 1 et seq., U.L.A. Fiduciaries Refs & Annos. (2008), Table of Jurisdiction Wherein Act Has Been Adopted.; As of May, 2008, the following states had adopted some form of the Uniform Fiduciaries Act: Ala., Ariz., Colo., D.C., Haw., Idaho, Ill., Ind., La., Md., Minn., Mo., Nev., N.J., N.M., N.Y., N.C., Ohio, Pa., R.I., S.D., Tenn., Utah, V.I., Wis., Wyo.

53 Unif. Prudent Inv. Act (1994) §§ 1 et seq., U. L. A. Prudent Inv. Refs & Annos., Table of Jurisdiction Wherein Act Has Been Adopted.; As of May, 2008 the following states had adopted some form of the Uniform Prudent Investor Act: Alaska, Ariz., Ark., Cal., Colo., Conn., D.C., Fla., Haw., Idaho, Ill., Ind., Iowa, Kan., Me., Mass., Mich., Minn., Miss., Mo., Mont., Neb., N.H., N.J., N.M., N.Y., N.C., N.D., Ohio, Okla., Or., Pa., R.I., S.C., Tenn., Tex., Utah, Vt., V.I., Va., Wash., W.Va., Wyo.

54 Id. at § 1(a).

55 Unif. Fiduciaries Act (1922) § 1, U.L.A. Fiduciaries Refs & Annos. (2008).

Thus, unless the school district is already considered a fiduciary with respect to the 403(b) plan, or unless a state's language specifically provides otherwise, these acts are more likely to interpret existing fiduciary duties than to apply new ones.

TRUE OR FALSE: Starting in 2009, a 403(b) plan sponsor can ignore any provider deselected before 2009.

False. Generally, a plan sponsor maintaining a plan on 1/1/09 must make reasonable good faith efforts to include providers deselected between 1/1/05 and 12/31/08 in the plan, but only with respect to individuals who are current employees as of 1/1/09. This does not mean the plan sponsor is required to allow either contributions or exchanges to these providers. It does mean that the affected contracts and accounts must be coordinated with other contracts and accounts under the plan with respect to such requirements as loans and hardship distributions.

Conclusion:

What does all of this mean, for answering the question of whether there are fiduciary duties under public employer 403(b) plans?

- If they exist, they do not come from the Code or from ERISA, nor are they likely to come from the Investment Adviser's Act. As a general matter, then, that leaves the issue to state law.
- Employers and their counsel should carefully review applicable state laws, especially those that commentators suggest could impose fiduciary duties on their 403(b) plans, since:
  - Many states have imposed significant limitations either on a public school's potential liabilities under the plan generally, or on their ability to restrict investment products, which may be controlling even if the employer is considered to be a fiduciary generally with respect to its employees.
  - Laws governing state pension systems often will not apply to a public school's 403(b) plan.
  - Other more general state laws, such as those governing fiduciary or prudent investing, generally apply if an individual is already a fiduciary, but do not themselves confer such fiduciary status.
- The bottom line: public schools should steer away from broad generalizations, and consult with their trusted legal counsel.