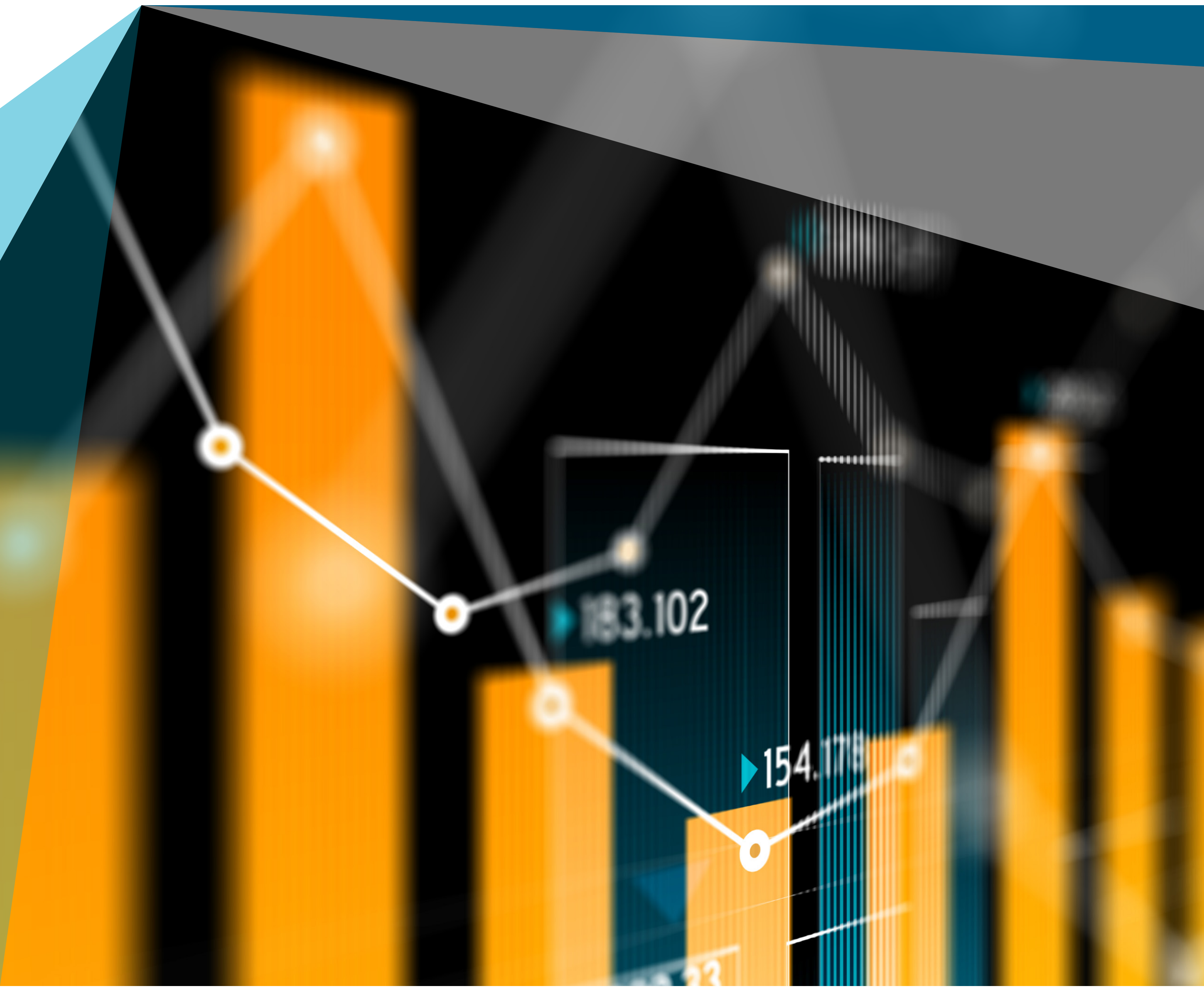
MARSH

FINPRO Practice

GLOSSARY OF FIDUCIARY LIABILITY INSURANCE TERMS



SOLUTIONS…DEFINED, DESIGNED, AND DELIVERED.

MARSH & McLENNAN COMPANIES

This glossary is intended to help industry professionals understand concepts related to fiduciary liability insurance programs.

For more information on the below terms and other risk and insurance issues, please visit marsh.com or contact your Marsh representative.

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# #

401(K) PLAN

A type of *defined contribution plan*. Under subsection 401(k) of the Internal Revenue Code, an employee can make contributions into a 401(k) plan from his or her paycheck on a pre-tax basis, with the employee often choosing investments based on options provided under the plan and paying associated expenses. In some plans, the employer matches the employee's contributions up to a certain percentage. 401(k)s are one of the most prevalent types of employer-sponsored pension plans in the US.

Also see: *Excessive Fee Litigation.*

403(B) PLAN

A type of defined contribution plan, similar to a *401(k) plan*, as defined under subsection 403(b) of the Internal Revenue Code. 403(b) plans are sponsored by nonprofit companies, religious groups, school districts, and governmental organizations for their employees. Most 403(b) plans are subject to *ERISA* if they are sponsored by private tax-exempt employers.

Also see: *Church Plans* and *Excessive Fee Litigation*.

404(C)

The ERISA section that permits employees to direct the investment of their defined contribution accounts (such as 401(k) plans) and offers plan fiduciaries a safe harbor when such self-direction results in investment losses.

To qualify for safe harbor protection, a plan must meet specific requirements regarding provided information about investment options and the ability to move balances between those options on a reasonably frequent basis.

Click here for more information.

457 PLAN

A type of *nonqualified*, *deferred compensation plan* established by state and local governments and tax-exempt organizations, similar to a *401(k)*, as defined under subsection 457 of the Internal Revenue Code.

502(i) ERISA PENALTIES

See: *ERISA Civil Penalties.*

502(c) ERISA PENALTIES

See: *ERISA Civil Penalties.*

502(g) PLAINTIFF ATTORNEY FEES

Legal fees and costs that a party to an *ERISA* matter may be able to recover in addition to any award or settlement in a civil action brought by a plan participant, beneficiary, or fiduciary.

Click here for more information.

502(l) ERISA PENALTIES

See: *ERISA Civil Penalties.*

4975 CIVIL PENALTIES

See: *ERISA Civil Penalties.*

A

ADMINISTRATOR (EMPLOYEE BENEFIT PLANS)

A person designated by the plan document to run the plan, as defined under *ERISA*. If an administrator is not designated, the *plan sponsor* is deemed to be the plan administrator.

ERISA requires administrators to notify plan participants in writing of the most important facts they need to know about their retirement and health benefit plans, including plan rules, financial information, and documents on the operation and management of the plan. This is called the *summary plan description*.

Click here for more information.

AFFORDABLE CARE ACT (ACA)

See: *Patient Protection and Affordable Care Act (PPACA)*

ASSET REVERSION

The recoupment of plan assets in excess of those required to pay accrued benefits by a sponsoring employer following the termination of an overfunded plan. Assets recovered through reversion are subject to regular corporate income tax plus an added 20% or 50% surcharge, depending on the type of successor retirement arrangement that is provided for employees.

C

CAFETERIA PLAN

A type of welfare *benefit plan*, governed by Section 125 of the Internal Revenue Code, which allows an employee to contribute a certain amount of his or her gross income to a designated "account" before taxes are calculated. This account can be used to reimburse the employee for insurance premiums or medical or dependent care expenses.

CASH BALANCE PLAN

A type of hybrid *defined benefit plan* that defines its benefit in terms more characteristic of a defined contribution plan — for example, as a set percentage of the employee's yearly compensation plus interest charges.

Changes in the value of a cash balance plan's investments do not directly affect the benefit amounts promised to participants. Therefore, the investment risks are borne solely by the employer.

Cash balance plans are often created by changing (or converting) a traditional defined benefit plan's promised benefit. Traditionally, these plan conversions have resulted in significant claims being filed under *fiduciary liability insurance policies*, which can be costly even in instances when defendants prevail.

Click here for more information.

CHURCH PLAN

A plan established and maintained by, or otherwise affiliated with a church on behalf of its employees.

ERISA protects all private-sector pension plans with the exception of church plans. Benefit plans sponsored by churches have a one-time, irrevocable right to elect to be covered by *ERISA*. Most do not make this election.

Along with other non-ERISA plans, church plans are subject to the state trust law under which they were established.

Click here for more information.

CONSOLIDATED OMNIBUS BUDGET RECONCILIATION ACT (COBRA)

A federal law designed to permit individuals who would otherwise lose their health insurance coverage to continue coverage through their employers or former employers at group rates if they are willing to pay the full premium themselves.

All companies that have averaged at least 20 full-time employees over the past calendar year must comply with COBRA regulations.

CO-FIDUCIARY LIABILITY

The duty, under *ERISA*, of plan *fiduciaries* to mind the business of their fellow *fiduciaries* and take action when becoming aware of facts indicating that those others have, or may have, engaged in a breach of their fiduciary duties.

Click here for more information.

CORPORATE TRUSTEE COMPANY

In the UK and other European countries, an entity that is assigned the responsibility for administration of a pension scheme and ensuring that members' interests are protected. A corporate trustee may be a subsidiary of the sponsor organization or an associated company.

D

DEFERRED COMPENSATION PLAN

An arrangement in which a portion of an employee's earned income is paid out at a later date. Typically, such a plan involves a highly compensated employees. Examples of types of deferred compensation plans include pensions, retirement plans, and employee stock options.

See: *Nonqualified Plans.*

DEFINED BENEFIT (DB) PENSION PLAN

A type of *pension plan* funded by an employer that promises the plan participant a specific monthly benefit at retirement.

An advantage of DB plans is that they are insured in the US by the *Pension Benefit Guaranty Corporation (PBGC)*, with the employer paying the PBGC a premium based on headcount and the funding status of the DB plan.

See: *De-risking Strategies.*

DEFINED CONTRIBUTION (DC) PENSION PLAN

A type of *pension plan* that has plan participants define or designate the pretax deductions from their paychecks that they wish to contribute, per pay period (subject to plan and statutory limits). In many cases, the participant is responsible for choosing how their contributions are invested. An employer may add to a participant's account, in some cases by matching a certain percentage of the employee's contributions.

At retirement, DC plan participants receive the balance in their accounts, reflecting the contributions, investment gains or losses, and any *fees* charged against their accounts.

401(k) plans are a popular type of defined contribution plan. Other examples include *employee stock ownership plans* and *profit sharing plans*.

See: *Pension Plans.*

DELINQUENT FILER VOLUNTARY COMPLIANCE PROGRAM

A program under the *Department of Labor*'s Employee Benefits Security Administration (EBSA) that provides plan administrators with the opportunity to pay reduced civil penalties for voluntarily complying with annual reporting requirements. The purpose of the program is to encourage pension and welfare plan administrators to file overdue annual reports (Form *5500*).

DEPARTMENT OF LABOR (DOL)

The US federal government agency that administers reporting, disclosure and fiduciary requirements under *ERISA*. The DOL may directly bring civil actions under *ERISA* to enforce the law's fiduciary duty provisions.

DE-RISKING STRATEGIES

Strategies that plan sponsors may pursue to reduce the potentially substantial financial exposure they could incur in meeting their benefit promises, whether these arise from *welfare benefit* or *pension plans.*

For health care plans, this may mean a focus on consumer-driven health care, with high-deductible health plans and health savings accounts.

For *defined benefit plans*, which involve substantial funding risks for plan sponsors, the need to juggle assets and liabilities, and market volatility, this may mean converting to a *cash balance plan*, freezing or terminating plans, or transferring liabilities to an annuity provider.

Click here for more information.

E

EMPLOYEE BENEFIT LIABILITY (EBL) EXTENSION

An extension that is typically found in general liability (GL) insurance policies that largely mirrors the coverage for alleged errors or omissions in plan administration found in *fiduciary liability insurance policies*.

EMPLOYEE PLANS COMPLIANCE RESOLUTION SYSTEM (EPCRS)

An *IRS* program that allows plan sponsors to remedy their mistakes and avoid the consequences of plan disqualification (or, in the case of a *403(b) plan*, the consequences of disqualification of a plan's annuity contracts or custodial accounts of employees).

Under the EPCRS, three programs exist to allow plan sponsors to correct mistakes:

1. The self-correction program (SCP) permits a plan sponsor to correct certain plan failures without contacting the IRS or paying any fee.
2. The voluntary correction program (VCP) permits a plan sponsor to, any time before audit, pay a fee and receive IRS approval for correction of plan failures.
3. The audit closing agreement program (audit CAP) permits a plan sponsor to pay a sanction and correct a plan failure while the plan is under audit.

EMPLOYEE STOCK OWNERSHIP PLAN (ESOP)

A type of defined contribution plan designed to invest primarily in the stock of the sponsoring employer. The US Congress authorized the creation of ESOPs as one method of encouraging employee participation in corporate ownership.

EMPLOYEE RETIREMENT INCOME SECURITY ACT OF 1974 (ERISA)

A US federal law that sets minimum standards for most voluntarily established *pension* and *welfare benefit plans* in private industry to provide protection for individuals covered by these plans.

ERISA does **not** require any employer to establish a retirement or welfare benefit plan. It only requires that established plans meet certain minimum standards. Plans that meet ERISA standards are referred to as *qualified plans*.

Generally, ERISA does not cover retirement plans established or maintained by government entities, churches, or certain other religious organizations for their employees or plans which are maintained solely to comply with applicable workers' compensation, unemployment, or disability laws.

ERISA also does not cover plans maintained outside the US primarily for the benefit of nonresident aliens or unfunded excess benefit plans.

Sometimes referred to as a "sword and a shield," ERISA's limited statutory remedies can be a boon for plan sponsors. In the context of welfare benefit plans, for example, if a benefit is determined to have been wrongful denied, resulting in tragic consequences, the sole ERISA remedy is the amount of benefit that should rightfully have been paid (meaning **no** punitive damages and **no** remedy for any resulting harm due to the initial wrongful benefit denial).

Click here for more information.

> In *Fiduciary liability* insurance policies, "ERISA" is usually defined as also including similar federal, state, local or common law, so that coverage extends to non-ERISA plans.

See: *Church Plans.*

ERISA BOND (ERISA FIDELITY BOND)

A type of insurance mandated by *ERISA* that protects a plan against losses resulting from fraudulent or dishonest acts of those covered by a bond.

ERISA sets out specific coverage provisions for ERISA bonds and annually determines the insurance companies permitted to issue an ERISA bond (or bond rider onto a firm's own fidelity bond).

> ERISA bonds are often confused with fiduciary liability insurance, which covers alleged ERISA breaches of fiduciary duty. Mandated ERISA bonds, by contrast, cover the theft of plan assets.

Click here for more information.

ERISA BREACH OF FIDUCIARY DUTY

A set of standards of conduct under *ERISA* for those who manage an employee benefit plan and its assets. *Fiduciaries* that do not follow the required standards of conduct may be held personally liable for violations or breaches of their duties to plans and their beneficiaries.

For example, if a plan loses money due to a breach of its duties, fiduciaries might be required to personally restore the losses resulting from their improper actions.

In addition to setting a prudent expert standard of care, *ERISA* creates the potential for *co-fiduciary liability* where one *fiduciary* may be liable for the actions of another.

ERISA CIVIL PENALTIES

- **502(c):** Penalties for the failure to provide plan documents.
- **502(i):** A civil penalty on prohibited transactions involving welfare plans and nonqualified pension plans. The basic penalty is up to 5% of the amount involved in the prohibited transaction, with a second penalty of up to 100% if the transaction is not corrected within the "correction period."
- **502(l):** A 20% penalty of the "applicable recovery" amounts recovered for a plan pursuant to a settlement agreement with the DOL or a court order resulting from a judicial proceeding instituted by the DOL. The DOL interprets Section 502(l) as a mandatory provision, giving it no discretion in the imposition of the penalty.
- **4975:** A 15% excise tax on the amount involved in a prohibited transaction. For example, the failure to deposit deferrals in the plan once they have become plan assets is, in effect, a loan from the plan to the sponsoring employer and is thus a prohibited transaction.)
- **Health care reform penalties:** The Affordable Care Act includes a mandate for certain large employers to either offer qualified and affordable health benefits or pay a tax penalty. Beginning in 2015, certain employers with 50 or more full-time equivalent employees that do not provide affordable health care coverage may be assessed a penalty if at least one full-time employee qualifies for a premium tax credit and uses it to purchase coverage from a health insurance exchange.
- **Pension Protection Act (PPA) penalties:** The PPA gave the Labor Department the authority to assess monetary penalties against plan administrators for:
  - Failure to notify participants and beneficiaries of their right to divest employer securities.
  - Failure to disclose certain forms of benefit distributions, actuarial reports, and financial reports.
  - Failure to notify contributing employers to multiemployer plans of their potential withdrawal liability.
  - Failure to provide notice of participants' rights and obligations under automatic contribution arrangements.

ERISA FIDUCIARY

As respects an *ERISA* plan, any person who:

- Exercises any discretionary authority or control over the management of a plan or the management or disposition of its assets.
- Renders investment advice for a fee or other compensation with respect to the funds or property of a plan, or has the authority to do so.
- Has any discretionary authority or responsibility in the administration of a plan.

Fiduciary status is based on the functions performed for the plan, not just a person's title.

See: *Co-fiduciary, Named Fiduciary*.

ERISA FIDUCIARY DUTIES

Specific responsibilities of *ERISA* fiduciaries, who are subject to the *prudent-expert rule* when fulfilling their duties to act on behalf of plan participants and their beneficiaries.

These duties and responsibilities include:

- Acting solely in the interest of plan participants and their beneficiaries and with the exclusive purpose of providing benefits to them.
- Carrying out their duties prudently.
- Following the plan documents (unless inconsistent with *ERISA*).
- Diversifying plan investments.
- Paying only reasonable plan expenses.

ERISA PLAN

An employee benefit plan that meets the standards set by the Employee Retirement Income Security Act of 1974. Whether providing *welfare benefits* or a *pension*, to be qualified under ERISA, plans must have the following, among other items:

- A written plan document that describes the benefit structure and guides day-to-day operations.
- A trust fund to hold the plan's assets.
- A recordkeeping system to track the flow of monies going to and from the retirement plan.
- Documents to provide plan information to employees participating in the plan and to the government.

A *qualified plan* is an ERISA plan.

ERISA PREEMPTION

The concept that *ERISA* specifically "supersede[s] any and all State laws insofar as they may now or hereafter relate to any employee benefit plan." The one major exception to this is for state-based insurance law, where applicable.

EXCESS BENEFIT PLAN

A *nonqualified plan* that provides more retirement income or *welfare benefits* to employees than permitted under an *ERISA qualified plan*.

EXCESSIVE FEE LITIGATION

A line of *ERISA* breach of fiduciary duty cases alleging that the *fees* paid by plan participants, typically in 401(k) or 403(b) defined contribution plans, have not been properly disclosed and/or are excessive when measured against the services provided.

The defendants in these matters could include the plans themselves, plan sponsors, plan *fiduciaries* and *administrators*, and service providers that receive *fees*.

> While currently seemingly confined to claims brought in the US, global employers could begin to see similar allegations brought in relation to local plans outside the US in circumstances where fees are being paid by plan participants.

Click here for more information.

F

FEES

One of several factors fiduciaries must consider in selecting plan service providers and investment options.

When fees for services are paid out of plan assets, *fiduciaries* will want to understand the fees and expenses charged and the services provided and ensure that they are properly disclosed to plan participants.

While *ERISA* does not specify a permissible level of fees, it does require that fees charged to a plan be "reasonable." After careful evaluation during the initial selection of service providers and investment options, a plan's fees and expenses should be monitored to determine whether they remain reasonable.

FIDUCIARY LIABILITY INSURANCE

A type of liability insurance that covers *fiduciaries* of privately-sponsored pension and *welfare benefit plans* for alleged breaches of fiduciary duty, along with alleged errors or omissions in plan administration. Coverage is extended to both *plans* and *plan sponsors.*

While not mandated under *ERISA*, like the *ERISA fidelity bond*, due to the potential for personal liability for fiduciaries, fiduciary liability insurance is commonly purchased and generally strongly recommended by counsel, brokers, and other advisors.

FIDUCIARY OUTSOURCING

The naming of a third party as a designated fiduciary, which is sometimes done by *plan sponsors*. *ERISA* specifies that each plan identify a *named fiduciary* and further provides that the named fiduciary may specify or designate others to carry out fiduciary responsibilities.

When a *named fiduciary* designates another fiduciary to carry out its responsibilities, it generally retains liability only for the designation itself, the prudent selection, and ongoing monitoring of this individual or entity.

FIDUCIARY RULE

A *Department of Labor* rule that defines a "fiduciary" as anyone who provides investment advice to a plan. Although the rule — which is meant to protect consumers — mostly impact financial services companies, it could also affect plan sponsors.

As of this writing, the fiduciary rule has been vacated by a court and is not being enforced by the DOL. Click here for more information.

FORM 5500 ANNUAL RETURN/REPORT

A form that plan administrators are generally required to file with the US federal government. The 5500 reports information about plans and their operation that is used by the *Department of Labor*, *Internal Revenue Service*, and *Pension Benefit Guaranty Corporation*.

These disclosures are made available to participants and the public. Depending on the number and type of participants covered, filing requirements may vary. Click here to access the forms.

H

HEALTH CARE REFORM PENALTIES

See: *ERISA Civil Penalties.*

HEALTH INSURANCE PORTABILITY AND ACCOUNTABILITY ACT OF 1996 (HIPAA)

A US law intended to protect the confidentiality and security of health care information. The law includes data privacy and security provisions to safeguard participant and beneficiary medical information.

I

INTERNAL REVENUE SERVICE (IRS)

A US federal government agency that administers funding, participation, and vesting standards of *ERISA* and is responsible for ensuring compliance with the ERISA Internal Revenue Code sections.

K

KSOP

A defined contribution plan that combines an *Employee Stock Ownership Plan* into a *401(k) plan*. In a KSOP, company matching contributions are typically made in company stock rather than cash. KSOPs benefit companies by reducing expenses that would arise by separately operating an *ESOP* and *401(k)* retirement plans.

Click here for more information.

L

LABOR MANAGEMENT RELATIONS ACT (LMRA)

A US law that provides a federal right of action and allows an employee to sue his or her employer for breach of contract even if the employer's alleged conduct is also an unfair labor practice prohibited by the National Labor Relations Act (NLRA)." This is specifically covered under Section 201 of the LMRA.

> This may be relevant where plan benefits have been negotiated under a collective bargaining agreement. A number of benefit cases have been brought under the LMRA rather than ERISA — so some fiduciary liability insurance policies expressly extend coverage to these claims. Even in suits brought under ERISA, courts may refer to LMRA actions to determine whether it should apply.

Click here for more information.

M

MONEY PURCHASE PLAN

A type of *defined contribution plan* similar to a profit-sharing plan, except that contribution amounts are fixed rather than variable. In a money purchase plan, employers are required to make annual contributions to each employee's account regardless of the company's profitability for the year.

MULTI-EMPLOYER (TAFT-HARTLEY) PLAN

A collectively bargained plan maintained by more than one employer, usually within the same or related industries, and a labor union.

Most multi-employer plans are jointly administered and governed by a board of trustees, with labor and management equally represented. The board of trustees normally makes decisions about the plan's benefit structure. The bargaining parties negotiate a contribution rate and the trustees translate that rate into a benefit. Decisions to increase benefits or change the plan are also typically made by the board of trustees. In some industries (especially mining and segments of trucking), employers and unions fix the benefit levels through collective bargaining.

The costs of administering a plan, including *fiduciary liability insurance*, are generally paid from plan assets.

MULTIPLE EMPLOYER PLAN (MEP)

A plan adopted by two or more employers that are unrelated for income tax purposes. There are three types of MEPs.

1. A plan sponsored by a professional employer organization that is adopted by the PEO's clients.
2. A plan sponsored by an industry or trade group to be adopted by the group's members.
3. A plan co-sponsored by participating employers with no relationship to or connection other than participating in a common plan.

N

NAMED FIDUCIARY

A person or entity named in a written plan, or chosen through a process described in the plan, that is assigned control over the plan's operation. A named fiduciary can be identified by office or name. A named fiduciary could be an administrative committee, a company's board of directors, or the *plan sponsor*.

NONQUALIFIED PLAN

A type of employer-sponsored *retirement plan* that falls outside of *ERISA* guidelines, typically because it would provide benefits in excess of those permitted under an *ERISA* plan and/or is designed to benefit primarily highly compensated employees.

As most *nonqualified deferred compensation* arrangements are unfunded, employers promise to pay nonqualified plan participants future benefits, without setting aside the funds for the employee; some may use a *rabbi trust* to fund all or some of the benefits that are ultimately due.

P

PATIENT PROTECTION AND AFFORDABLE CARE ACT (PPACA)

A federal law with three primary goals:

1. To make affordable health insurance available to more people. The law provides consumers with subsidies (premium tax credits) that lower costs for households with incomes between 100% and 400% of the federal poverty level.
2. To expand Medicaid to cover all adults with income below 138% of the federal poverty level. Not all states have expanded their Medicaid programs, however.
3. To support innovative medical care delivery methods designed to lower the costs of health care generally.

PENSION BENEFIT GUARANTY CORPORATION (PBGC)

A nonprofit, federally created corporation that guarantees payment of certain *defined benefit* pension benefits if a plan is terminated with insufficient money to pay benefits (a distress termination). Oftentimes, but not always, this occurs when an employer goes bankrupt.

The PBGC also has the power to force an involuntary termination of a *defined benefit plan* when it believes that the plan's continued operation will lead to an inevitable increase in underfunded benefits.

Click here for more information.

PENSION PLAN

A plan designed to provide retirement income to employees or one that results in a deferral of income by employees to periods extending beyond termination of employment. There are two main types of retirement plans:

- *Defined benefit (DB) plans:* An employer guarantees to an employee a stream of payments, often based on years of service (generally received monthly, upon retirement). DB plans are insured by the *Pension Benefit Guaranteed Corporation*; employers pay the *PBGC* premiums based on headcount and the funding status of DB plans.
- *Defined contribution (DC) plans:* Participants designate how much money they would like to contribute to these plans per pay period (subject to plan and statutory limits). Examples include profit-sharing plans, money purchase plans, and 401(k) plans.

Click here for more information.

PENSION PROTECTION ACT OF 2006 (PPA)

A US law that introduced several reforms to strengthen the overall pension system and hold accountable companies with underfunded pension liabilities.

Click here for more information.

PENSION SCHEME

See: *Pension Plan.*

PLAN ASSETS

Generally, stocks, bonds, and other investments that have been segregated and restricted (usually in a trust) so they can only be used to provide for post-retirement benefits.

Plan assets include amounts contributed by employers (but not amounts accrued and unpaid), amounts contributed by plan participants for a contributory plan, and amounts earned from investing the contributions, less benefits, income taxes, and other expenses incurred.

PLAN ADMINISTRATOR

See: *Administrator (Employee Benefit Plans).*

PLAN DISQUALIFICATION

The determination by the *IRS* that a plan fails to meet ERISA's requirements. When an *ERISA qualified plan* is disqualified, the plan's *trust* loses its tax-exempt status and becomes a nonexempt trust. Plan disqualification affects three groups:

1. Employees.
2. Employers.
3. The plan and its trust.

Click here for more information.

PLAN DOCUMENT

See: *Summary Plan Description.*

PLAN SPONSOR

Usually, the company or employer that sets up a plan for the benefit of the organization's employees.

PROHIBITED TRANSACTIONS

Certain transactions prohibited under the law to prevent dealings with parties (parties in interest) that may be in a position to exercise improper influence over the plan. Fiduciaries are prohibited from engaging in self-dealing and must avoid conflicts of interest that could harm the plan. Parties in interest include employers, unions, plan fiduciaries, service providers, and statutorily defined owners, officers, and relatives.

PROFIT-SHARING PLANS

A type of *defined contribution plan* that gives employees a share in the profits of a company (for example, a percentage of a company's profits based on its quarterly or annual earnings). In a profit-sharing plan, contributions from the employer are discretionary.

PRUDENT EXPERT RULE

A rule that outlines the standard of care for *ERISA fiduciaries*. Prudent experts must act with "the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims."

Click here for more information.

Q

QUALIFIED PLAN

An employer-sponsored plan that meets the requirements established by the *Internal Revenue Service* and the US Congress under *ERISA*. Examples include *defined benefit pension plans* (including cash balance plans), *profit-sharing plans*, money purchase plans, *cash balance plans*, simplified employee pension plans, and *401(k)s*.

A qualified plan is entitled to the tax benefits and protections of the *Employee Retirement Income Security Act*.

See: *Plan Disqualification.*

R

RABBI TRUST

A trust established by an employer to provide a source of funds that may be used to satisfy the employer's obligation to executives under a nonqualified benefit plan. The trust is referred to as a rabbi trust because the first *IRS* letter ruling with respect to this type of trust involved a rabbi.

S

SETTLOR ACTS

Business decisions made by employers, as opposed to *fiduciary* actions, that affect plans. For example, decisions to establish plans, determine benefit packages, include certain features, amend plans, and terminate plans are business decisions generally not governed by *ERISA*.

When making these decisions, an employer is acting on behalf of its business, not the plan, and therefore is not a *fiduciary*. However, when an employer (or someone hired by the employer) takes steps to implement these decisions, that person is acting on behalf of the plan.

> To clarify coverage, some fiduciary liability policies include specific wording addressing coverage for settlor claims (which usually begin as allegations of ERISA breaches of fiduciary duty).

SIMPLIFIED EMPLOYEE PENSION PLAN (SEP)

A type of *defined contribution plan* in which an employer makes contributions on a tax-favored basis to individual retirement accounts (IRAs) owned by employees. In a SEP, the employer, not the employee, reaps the tax benefits of the retirement contribution. SEP IRAs are *ERISA qualified.*

STOCK BONUS PLAN

A type of *defined contribution profit-sharing plan* to which employers contribute company stock. These are generally considered to be qualified retirement plans, governed by *ERISA*.

STOCK PURCHASE PLAN (ALSO KNOWN AS EMPLOYER STOCK PURCHASE PLAN OR ESPP)

A plan that allows a company's employees to purchase its stock. Under a qualified stock purchase plan, employees buy shares in the employer's stock; the stock may be offered at a fixed price (usually below market) and paid for in full by the employees. In a nonqualified plan, senior management or other key personnel can purchase employer stock, but certain restrictions apply:

- The stockholder must be employed for a particular length of time.
- The employer has the right to buy back the stock.
- Stockholders cannot sell the stock for a specific time period.

SUMMARY PLAN DESCRIPTION (SPD)

A plain language explanation of a plan that is comprehensive enough to apprise participants of their rights and responsibilities. An SPD also informs participants about plan features and what to expect of the plan.

- Among other things, an SPD must include information about:
- When and how employees become eligible to participate.
- The source of contributions and contribution levels.
- The vesting period, meaning the length of time an employee must belong to a plan to receive benefits from it.
- How to file a claim for those benefits.
- A participant's basic rights and responsibilities under *ERISA*.

This document is given to employees after they join the plan and to beneficiaries after they first receive benefits. SPDs may also be redistributed periodically and provided on request.

T

TARGET-DATE FUND

Found in *401(k) plans*, an investment option that seeks to grow assets over a specified period of time for a targeted goal. Target-date funds are usually named by the year in which the participant plans to begin using the assets.

The asset allocation of a target-date fund is a function of the specified timeframe available to meet the targeted investment objective. A target-date fund's risk tolerance become more conservative as it approaches its objective target date.

Click here for more information.

THRIFT SAVINGS PLAN (TSP)

A type of *defined contribution plan* designed to give federal employees and members of the uniformed services some of the same retirement savings benefits offered to workers in the private sector. The TSP was established by Congress in the Federal Employees' Retirement System Act of 1986 and is administered by the Federal Retirement Thrift Investment Board.

TITLE I OF ERISA

A section of *ERISA*, administered by the *Department of Labor*, that includes regulations relating to reporting, disclosure, vesting, participation, and funding of *ERISA plans.*

TITLE II OF ERISA

A section of *ERISA*, administered by the *IRS*, that sets standards for *pension benefit plans* to qualify for favorable tax treatment.

TITLE III OF ERISA

A section of *ERISA* that addresses jurisdictional matters and coordination of enforcement and regulatory activities by the *DOL* and *IRS*.

TITLE IV OF ERISA

A section of *ERISA*, administered by the *Pension Benefit Guaranty Corporation*, that covers the insurance of *defined benefit pension plans.*

TOP-HAT PLAN

A *nonqualified plan* that is unfunded and maintained primarily for the purpose of providing *deferred compensation* or *welfare benefits* for management or a select group of highly compensated employees.

TRUST

A fiduciary relationship in which one party gives another party the right to hold title to property or assets for the benefit of a third party. *ERISA* generally requires that plan assets be held in trust so that they are protected from claims of the employer.

TRUSTEE

An entity or individual who holds the assets of a *qualified plan* in trust. Trustees are either designated in the plan document or appointed by another *fiduciary*, typically the employer who sponsors the plan.

V

VESTING

A process through which plan participants earn a nonforfeitable right to accrued benefits (generally under a *pension plan*) based on their completion of years of service as specified under a plan's vesting provisions.

Non-vested benefits are forfeited by participants on separation of services. Employee contributions are immediately vested. Benefits under a health and welfare plan generally do **not** vest, but this varies depending on the actual plan wording.

VOLUNTARY EMPLOYEES BENEFICIARY ASSOCIATION (VEBA)

A type of tax-exempt trust used by its members and eligible dependents to pay for eligible health expenses. This plan is funded by an employer and does not require contributions from employees. However, employees must be covered by an employer-sponsored health plan to be eligible for VEBA benefits.

VEBAs are subject to some aspects of ERISA, but are not considered *qualified welfare benefit plans*. VEBA plans are considered welfare benefit plans under federal tax law and are tax-exempt under Section 501(c)(9) of the *Internal Revenue Code*. Employer contributions made to a VEBA plan are tax-deductible and have no limit.

VOLUNTARY FIDUCIARY CORRECTION PROGRAM (VFCP)

A *Department of Labor (DOL)* program that encourages employers to comply with *ERISA* by voluntarily self-correcting certain violations.

The program covers 19 specific transactions, including failure to timely remit participant contributions and some prohibited transactions with parties in interest. The *DOL* gives successful applicants immediate relief from payment of excise taxes under a class exemption.

W

WAIVER OF RECOURSE

A provision in an agreement or instrument which purports to relieve a fiduciary from responsibility or liability from any responsibility, obligation, or duty under *ERISA*. Section 410(a) of *ERISA* generally prohibits any such provisions.

ERISA, however, permits the purchase of *fiduciary liability insurance* by plans, sponsors, and employers, provided that if purchased by a plan such insurance permits recourse by an insurer against the *fiduciary* in the case of a breach of fiduciary obligation (ERISA §410(b)(1)).

When fiduciary liability insurance premiums are paid for by plans (which is typical for multi-employer plans but not single employer plans), it is imperative that fiduciaries pay a portion of the premium so that *ERISA* does not require the insurer to retain a right of recourse.

WELFARE PLAN (ALSO KNOWN AS HEALTH AND WELFARE PLAN)

A type of plan that provides health, disability, or death benefits, prepaid legal services, vacation benefits, day care coverage, scholarship funds, apprenticeship and training benefits, or other similar benefits.

Unfunded benefits or payroll practices, such as vacation, holidays, overtime premiums, holiday gifts, and compensation paid for time not worked, are generally not included in welfare plans. Group-type voluntary insurance programs to which the employer makes no contribution are also excluded.


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