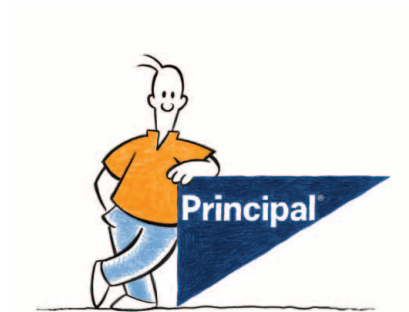


The Fiduciary Handbook

A Guide to Plan Sponsor and
Plan Fiduciary Responsibilities

[Excerpt]



Preface by Fred Reish, Nationally Known ERISA Attorney

This Handbook has been written for the men and women who have the responsibility for managing tax-qualified retirement plans. That is an important job... because the retirement standard of living of your participants will depend partially on the decisions that you make. If your job is well done, employees can retire with more money and have a better opportunity for a good quality of life in retirement.

Unfortunately, most discussions of retirement plan responsibilities focus on the fiduciary requirements, and potential liabilities, under the Employee Retirement Income Security Act of 1974 (ERISA), the federal law governing retirement plans. However, viewed properly, ERISA is a road map for successfully accomplishing the greater responsibility – the secure retirement of your employees.

The vast majority of decision-makers, such as yourself, successfully navigate ERISA's fiduciary waters without experiencing participant claims, Department of Labor (DOL) investigations, or lawsuits. This Handbook will help you enjoy the successes of a qualified retirement plan and avoid the legal pitfalls.

*As a decision-maker – a fiduciary – your first job is to **do what's right for the participants**. In fact, the most important legal requirement under ERISA is that you act solely in the interest of the participants and for the exclusive purpose of providing retirement benefits (and paying only reasonable expenses). Once you understand that rule and accept that responsibility, most of the remaining requirements of ERISA are logical and intuitive. One commentator has made the analogy, "When you are managing your mother's retirement money, you don't need to call a lawyer...you intuitively know what to do." If you bring that standard of care to supporting your employees' retirement benefits, you will have gone a long way toward satisfying your fiduciary requirements.*

*Of course, some retirement plan decisions are difficult – and may require an expertise that you do not have. In those cases, under ERISA, you can turn to outside advisers for help. Those would include the plan recordkeeper, investment provider, a financial professional or broker, an investment adviser...and, yes, even an ERISA attorney. You need to make sure that the adviser is competent and qualified, and you need to evaluate and understand the advice and information they give you. Then, you need to make a reasoned and informed decision for the benefit of your participants. Having done that, you will have satisfied ERISA's requirement that you engage in a "prudent process." Stated simply, **a prudent process requires that you look at the right information in the right way.***

As an attorney, I would be remiss if I did not advise you of the need to document your decisions and to place that document (e.g., minutes of a meeting or just a memo) in a due diligence file. That file should also include the information you reviewed and advice you received. The records should be kept for at least six years.

Sponsoring a retirement plan can, and should, be a win-win situation. If you combine a good plan service provider with the necessary services (such as an adviser, investment education, and so on), your organization will provide an attractive benefit to help retain your current employees and to attract new employees. In due course, those employees can accumulate meaningful retirement benefits.

While this Handbook primarily focuses on the legal responsibilities for participant-directed plans like 401(k) plans, it also discusses responsibilities for operating other types of retirement plans such as profit sharing, money purchase, and defined benefit plans. In fact, many of the basic principles apply to all types of qualified retirement plans.

*As you might imagine, as an ERISA attorney, I am particularly interested in the law and how it applies to the management of retirement plans. With that in mind, I have reviewed *The Fiduciary Handbook* for accuracy in its presentation of the law. **I am pleased to report that the Principal Financial Group® has done a good job of introducing and explaining ERISA's basic requirements for the management of retirement plans. Equipped with this information, you will be on your way to better understanding your responsibilities and therefore, to helping your organization, your employees, and yourself.***

I hope you enjoy these materials and profit from them.

A handwritten signature in black ink that reads "Fred Reish". The signature is written in a cursive, slightly stylized font.

Fred Reish

Reish Luftman Reicher & Cohen

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* Note: If you are working with a TPA, he/she fulfills this portion of the handbook.

Get Educated*

Take control of your fiduciary obligations.

For your employees, a retirement plan is among the most valuable benefits available. Plan sponsors, however, must be aware of their important legal responsibilities because almost all qualified plans are subject to ERISA rules.¹

While the laws governing retirement plans and their fiduciaries' responsibilities are complex, complying with them doesn't have to be stressful. It simply requires an awareness of the rules, an attention to the issues, and the use of quality advisers and service providers.

* Note: If you are working with a TPA, he/she fulfills this portion of the handbook.

¹ There are limited exceptions; for example, non-electing church and certain tax-exempt entity plans.



At The Principal®, we understand the unique needs of plan sponsors and their participants.² Our goal is to help you navigate ERISA requirements and to successfully manage your fiduciary obligations. As an industry leader with more than 60 years of retirement plan experience, we're committed to assisting the more than 45,000 plan sponsors³ who choose our expertise.

While this guide was developed for plan sponsors of defined benefit, defined contribution, and employer-sponsored 403(b) plans, it focuses primarily on participant-directed plans such as 401(k) and 403(b) plans except where noted.

The first section of this Handbook is designed to help educate you on:

- The role of an ERISA fiduciary
- The importance of choosing appropriate investment options
- The difference between participant education and advice
- The requirements for compliance with ERISA and the applicable regulations
- The management of your fiduciary responsibilities

By managing the plan in accordance with ERISA standards, plan sponsors can protect themselves from potential liability and help participants maximize their benefits.

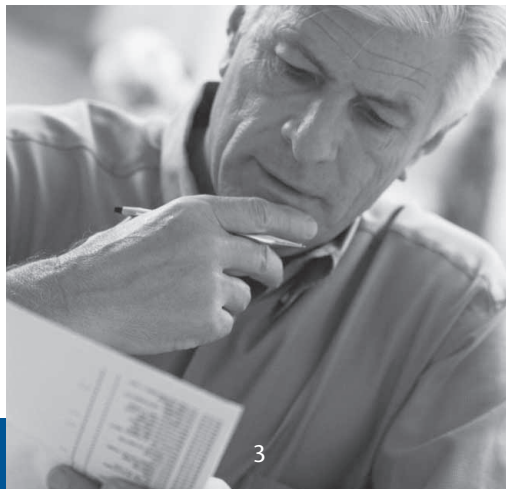
After reviewing this Handbook, we strongly encourage plan sponsors to consult with their financial professionals, attorneys, accountants, and other parties as needed.

² To make this Handbook easier to read, the term "participant" is used to refer to both participants and beneficiaries.

³ As of 9/30/07

Understanding How ERISA Protects Retirement Plan Participants

ERISA was enacted to protect participants' retirement savings by governing the operation and investment of most private sector retirement plans. The persons given the primary responsibility for managing the retirement plan investments are called **fiduciaries**. They are required to act in the best interests of their plan and its participants – and are held to exceptionally high standards. Failure to comply with these ERISA standards can result in the imposition of significant personal liabilities and penalties – for both the fiduciaries and the company that sponsors the plan.



Enforcing ERISA

While there are several enforcement mechanisms for ERISA, most plan sponsors operate their plans without penalties or lawsuits. Awareness of the rules and the use of quality service providers are keys to successfully managing your plan. The following groups are involved with ERISA standards enforcement, both directly and indirectly.

The Department of Labor's (DOL) Employee Benefits Security Administration (EBSA) focuses on whether fiduciaries have complied with their ERISA duties. For example, during the investigation of a plan, the EBSA looks closely at the timing of salary deferral deposits, the reasonableness of plan expenses, the prudence of investments, and any transactions involving closely related parties (e.g., the plan sponsor or its owners).

The Internal Revenue Service (IRS) oversees the application of the Internal Revenue Code (IRC) that establishes the rules for operating a tax-qualified retirement plan and enforces compliance with these rules through the auditing of plans. The discovery of serious rules violations can result in penalties and taxes. However, the IRS willingly assists plan sponsors by providing IRC education and approving plan documents.

The Pension Benefit Guaranty Corporation (PBGC), another federal agency, oversees defined benefit pension plans to monitor the adequacy of the funding of promised pension benefits – and insures a minimum level of pension benefits.

Participants can also indirectly enforce ERISA by filing claims for benefits or suing fiduciaries for breaches of their ERISA duties.

For more information, please contact a representative of the Principal Financial Group.

Defining a Fiduciary

A fiduciary is defined as any individual who:

- Is named in the plan document as a fiduciary or is appointed as a fiduciary in accordance with a procedure in the plan document
- Exercises any discretionary authority or control regarding the management of a retirement plan or its assets; or exercises any control over the management or disposition of a plan's assets
- Provides (or has any responsibility to provide) investment advice with respect to plan assets for compensation such as commissions
- Has any discretionary authority or responsibility for plan administration

Named fiduciaries have the authority to control and manage the operation and administration of the plan, including its investments. ERISA requires a retirement plan to have one or more named fiduciaries, one of which serves as **plan administrator** (the person or persons who are responsible for administering the plan). A named fiduciary can be an individual, group of individuals, or the employer/company – and must be designated in the plan document or in accordance with a procedure described in the plan document. A committee appointed to manage the plan under the terms of the plan document is also considered a named fiduciary.

Functional fiduciaries, generally speaking, are persons who exercise control over the plan or its investments – or give investment advice – but are not formally appointed to perform those roles. To be considered a functional fiduciary, a person must exercise discretionary control over the management of a plan or its assets; exercise any authority or control over the management or disposition of a plan's assets; exercise any discretionary authority for plan administration; or provide investment advice about plan assets for compensation.

Determining Who Isn't a Fiduciary

An individual isn't considered a fiduciary if he/she either isn't a named fiduciary; or isn't appointed or doesn't function as a fiduciary. Accountants, attorneys, consultants, and other persons who perform purely administrative functions within a framework of policies, interpretations, rules, practices, and procedures made by other persons aren't ordinarily fiduciaries. However, they can become functional fiduciaries if they take on any of the fiduciary responsibilities outlined by ERISA.

Understanding Plan Fiduciary Responsibilities

A fiduciary should operate a plan solely in the interests of its participants, according to the ERISA duty of loyalty, and must also comply with the requirements listed below.

Exclusive Benefit Rule: A fiduciary must act for the exclusive purpose of providing benefits and paying only reasonable plan expenses.

Prudent Person Rule: A fiduciary must perform his/her duties “with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with such matters would use [under similar circumstances].”

Regarding investment selection, this is sometimes called the “prudent expert” rule because fiduciaries are measured by the standard of a knowledgeable investor. In other words, a good faith effort without investment knowledge isn’t enough. To satisfy this rule, fiduciaries must engage in a prudent process by gathering all important information and analyzing it before making a decision.

If fiduciaries lack expertise in retirement investment matters, they should seek the advice of knowledgeable advisers. And, they should retain the information received and document their processes to protect themselves against potential breach of duty claims. For more information on this subject, see the section “Creating a Documented Process.”

Diversification Rule: To minimize the risk of investment losses, fiduciaries are required to diversify their plans’ investments. The diversification rule may not apply to certain plan types that hold qualifying employer securities (e.g., an Employer Stock Ownership Plan). When choosing investments, the fiduciaries should select investments with different objectives and risk/return characteristics. For participant-directed plans, a broad range of investment options should be offered so participants have the opportunity to build portfolios appropriate to their goals and risk tolerances.

Duty to Follow Plan Terms: Fiduciaries are required to act in accordance with the plan document to the extent they are consistent with ERISA rules. However, if a plan’s provisions would cause a violation of ERISA rules, fiduciaries are required to override the plan document.

For more information, please contact a representative of the Principal Financial Group.