

**Add More Teeth to Your Deferred Compensation Security-
*An Independent Third Party Fiduciary Can Add an Extra Layer of Protection***

**By William L. MacDonald
Chairman, President & Chief Executive Officer
Retirement Capital Group, Inc.**

Early one summer morning I received a phone call from an executive with a situation that could have been lifted from the business page of your local newspaper. Shareholders of a corporation are convinced their senior management team is taking them in the wrong direction, and they vote to remove them. It is an ugly situation to be sure, but not uncommon. Senior management participates in the Company's Nonqualified Deferred Compensation Plan (NQCP), which is funded with assets held in a so-called "Rabbi Trust." The former CEO files a claim for his terminated benefits under the Company's NQDC Plan.

But the Plan Committee, like those responsible for administering retirement plans and reviewing claims at most firms, consists of current employees (including the *new* CEO) beholden to the controlling shareholder group that ousted the ex-CEO. The Committee, therefore, rejects the ex-CEO's claim for termination benefits under the NQDC plan on the specious grounds that the ex-CEO violated one or more of the plans so-called "bad boy" clauses (such as going to work for a competitor or disclosing confidential information). Even though assets have been set aside in a "Rabbi Trust," and even though the ex-CEO did no wrong, he must now pursue a lengthy appeals process, mandated under the Employee Retirement Income Security Act (ERISA). The entire matter will likely end up in a costly litigation. In short, it could be years before the innocent ex-CEO sees a penny of his deferred compensation benefits from the "Rabbi Trust." Furthermore, because the assets in the "Rabbi Trust" remain subject to the claims of the Company's creditors, if the Company should suffer setbacks or go out of business during this period, the ex-CEO could end up with nothing.

NQDC plan participants want to be assured that their money will be there for them when they are entitled to receive it, which is why various "security devices" for such plans have become more important than ever to covered employees. The majority of companies with deferred compensation plans use funded "Rabbi Trusts," but they may not do the job without the right provisions.

To prevent unfortunate scenarios like the one outlined above, Retirement Capital Group, Inc. (RCG) recommends that your plan offer its participants a relatively new service, third-party plan fiduciary services – that, in fact, can represent an important added NQDC plan security device.

On the Outside Looking In

Under ERISA, all benefit plans must be overseen by administrators who have a fiduciary duty toward the plan, i.e., who are charged with making important discretionary decisions

concerning the plan, such as whether to deny or approve covered employees' claims for benefits under the plan. Many companies now outsource what are essentially "ministerial" functions of the plan – such as generating account statements, tracking results, etc. – to an outside trustee or third-party administrator. In fact, RCG has a valuation process to help you select the best administration for your plan. But when it comes to the key decisions, most firms' plan documents require the decisions to be made by a committee consisting of company employees. The committee typically hires investment managers to invest plan assets and make all benefit entitlement determinations themselves, directing a trustee to pay out benefits accordingly.

There can be several problems inherent in this approach. First, company employees may have neither the expertise nor the interest in fulfilling their committee duties, or they may not have an adequate understanding of the plan and its features. Secondly, company employees may not want to be exposed to fiduciary liability if they make mistakes. Third and most importantly, however, conflicts of interest may arise when current employees (who, it should be noted, may or may not be plan participants) are responsible for making decisions that can affect the benefits of fired former employees, as the ex-CEO learned to his chagrin.

An independent, third-party fiduciary can overcome these obstacles and provide a potent new type of benefit protection for covered employees. Had this feature been in place at his former company, the ex-CEO may still have faced a challenge to his claim, but the claim would have been decided by a neutral, outside party. The independent, third-party fiduciary would, in effect, function as an administrative law judge, reviewing the plan documents, weighing the merits of the case and making a finding of fact. Neither side gives up their appeal rights; if the fiduciary denies a claim for benefits, an employee must still exhaust the appeals procedure provided under ERISA before taking his case to court.

But because the decision is no longer in the hands of company employees, the nightmarish prospect of having a claim rejected due to specious allegations, raised in the midst of an often awkward if not downright hostile atmosphere, can be virtually eliminated. It also shields employees once they leave the company from unforeseen circumstances, such as change in control. (Returning to the ex-CEO, his company could have inserted the provision in the NQDC plan documents giving *him* the power to appoint a third-party fiduciary in the event of a change in control, which the company would then be powerless to dismiss.)

Overview of Fiduciary Functions

Typically, an independent, third-party fiduciary should:

- Interpret all plan and trust documents,
- Make benefit entitlement determinations,
- Direct the trustee regarding payment schedules,
- Verify whether plan or trust assets are actually held in the trust,

- Monitor the client's routine administration and operation of both the plan and trust.

In addition, for each plan year, a third-party fiduciary may conduct periodic on-site audits of plan record-keeping and plan assets, provide client and individual plan participants with annual reports regarding the operation and current funding status of the plan and monitor all plan documents and amendments and any changes in the tax laws.

On an as-needed basis, an independent, third-party fiduciary should also be prepared to take any actions necessary to enforce compliance with the plan and trust documents; take steps to enjoin any acts or omissions in violation of plan documents, the trust or ERISA regulations; make rules and regulations regarding plan and trust administration; and keep all plan and trust documents up-to-date, making sure all documents are revised and amended in a timely manner to reflect changes in the law or the company's circumstances.

An independent, third-party fiduciary will not, however, typically direct or advise the plan, trustee or individuals with respect to investment or valuation of trust assets, nor actually invest the assets or provide investment advice. In addition, a third-party fiduciary generally will not take responsibility for any failure by a company to file any information returns or failure to withhold or pay over any taxes, interest or penalties due or assessed with the plan, the trust or individual participants.

Conclusion

Any NQDC plan fiduciary must have the requisite experience and knowledge to make thoughtful, informed decisions on behalf of the plan and participating employees, and also be willing to exercise sound, independent judgments based on the facts and on the specific provisions of the plan. A neutral, third-party fiduciary may be better versed in the intricacies of nonqualified executive benefits than company employees, thus placing them in a better position to monitor funding of the benefit promise.

By relieving an in-house committee of its fiduciary responsibilities and liabilities (a fiduciary can be held *personally* liable for any errors or omissions or plan losses resulting from a breach or ERISA rules), an outsider is also better able to make often-problematic determinations about benefit entitlements without personal relationships clouding the process. Best of all, plan participants gain an extra measure of plan security and peace of mind knowing that their benefits will be there when they expect them to be, and won't be held up by a change of heart, a change in control or other factors and events beyond their control.

If your company never thought about bringing in a third-party "watchdog" for its NQDC plan fiduciary needs, now is the time to consider such a move, even if your NQDC benefits are funded with a "Rabbi Trust." The experts at RCG are uniquely qualified to consult with you on whether this innovative new service is right for your plan.