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Establish an Administrative Committee for Your ERISA Health and Welfare Benefit Plans

by Eric D. Altholz on March 15, 2021

The fiduciary standards of ERISA apply to all employee benefit plans that are subject to Title I of ERISA. The duty of loyalty, the duty of prudence, and the duty to administer a plan in accordance with its written terms apply equally to "employee welfare benefit plans" and "employee pension benefit plans," differences in specific fiduciary activities notwithstanding. This has been true since ERISA was signed into law 47 years ago, yet even the most compliance-oriented employers seem to apply a lighter fiduciary touch when it comes to welfare benefit plans. Most well-advised employers have robust fiduciary governance structures for their retirement plans built around administrative and investment committees, which have adopted written charters and meet regularly. Yet many of these same employers make important fiduciary decisions with respect to their welfare benefit plans – such as the selection and monitoring of health plan third-party administrators – on an ad hoc basis without any formal fiduciary structure. There are many reasons for this. But the time has now come to apply the key fiduciary governance principles and practices that have long been commonplace with respect to retirement plans to health and welfare benefit plans.

Why the difference in fiduciary governance practices?

There are many reasons why employers have paid more attention to fiduciary compliance for retirement plans than health and welfare benefit plans. The application of ERISA's fiduciary standards to retirement plans has been the subject of a continuous stream of federal regulations and other guidance, enforcement activity, and caselaw for many years. Litigation in particular has proven to be a highly effective motivator of compliant behavior. The many well-publicized federal cases – starting with seminal cases decided in the early 1980s and continuing through the recent wave of class action lawsuits against sponsors of 401(k) and 403(b) plans – attracted the attention of employers and their advisers and provided constant reminders of the importance of having a sound fiduciary governance framework.

Even without the external stimulus of litigation risk, employers have perceived that the stakes are high and somewhat quantifiable when it comes to fiduciary breaches in connection with retirement plans. Design differences aside, retirement plans have in common large accumulations of assets, with a massive industry devoted to investing those assets, keeping track of the benefits they are intended to fund, and the payment of those benefits to millions of employees over many years. The risks are many and they are easy to understand.

Health and welfare plans, by comparison, seem less fraught with risk. Even though health insurance companies rival retirement plan financial services firms in size, wealth, and clout, they pay benefits on a year-to-year basis under a contract: the employer and its employees pay monthly premiums and get medical benefits in exchange. Even though large employers with self-funded group health plans pay out tens of millions of dollars in medical claims and administrative expenses each year – often dwarfing employer contributions to their retirement plans – the accounts used to fund those expenses are typically spent down, with a reasonable reserve, each year. Special circumstances aside, there is rarely a need for long-term cash accumulation, and any assets that are invested would be invested in short-term highly liquid investments. So even though health benefits are at least as important to employees as retirement benefits, the stakes simply do not seem as high. In addition, other welfare benefits, such as group term life, long-term disability and so on, are almost always provided through insurance contracts that generally do not require a lot of hands-on engagement by the employer. Add to that the relative paucity of detailed guidance and litigation with implications for fiduciary activities, and it is not hard to understand why employers choose not to devote precious resources and attention to fiduciary governance activities for their health and welfare plans.

Why implement fiduciary compliance practices for welfare benefit plans now?

Nine years have passed since the Department of Labor ("DOL") finalized regulations under Section 408(b)(2) of ERISA, which mandate the disclosure of fees charged to retirement plans and plan participants by investment funds, investment managers, recordkeepers and other service providers. These disclosures form a critical element of the statutory exemption from prohibited transaction rules, which generally allow a party in interest (such as an investment manager) to provide services to a plan only if fees are reasonable. The Section 408(b)(2) disclosure regulations directly support the reasonable fee requirement by putting plan fiduciaries in a position to understand and evaluate these fees.

Before the disclosure regulations, fee arrangements were opaque and created opportunities for service providers to gain compensation in ways that even a sophisticated fiduciary may not understand. This made it difficult to determine whether the fees were reasonable. Those kinds of risks are present in the arrangement under which services are provided to health and welfare benefit plans as well, yet the Section 408(b)(2) fee disclosure regulations currently apply only to retirement plans, with a placeholder for analogous disclosures with respect to welfare benefit plans. New disclosure requirements contained in the Consolidated Appropriations Act of 2021 ("CCA") signal that Congress – and, presumably, the DOL – may be ready to extend disclosure obligations to welfare benefit plan service providers.

The CAA contains provisions that will require brokers and consultants to employer-sponsored group health plans to disclose to plan sponsors the fees they expect to receive and the services they will provide to earn those fees. The disclosure obligation applies to any broker or consultant that reasonably expects to receive $1,000 or more in direct or indirect compensation *from plan assets* for providing services to group health plans. (The question what constitutes "plan assets" in a self-funded group health plan is beyond the scope of this post but will be addressed on our blog later this month.) The services provided by brokers can cover a wide range of health plan needs, including selection of insurance products, claims administration, selection of pharmacy benefit managers and other vendors. Disclosure is also required for entities that provide consulting services such as assisting employers with plan design, pricing, cost analysis, the selection of third-party administrators ("TPAs"), and other administrative matters. The new disclosure requirements under the CAA, which take effect in December 2021, are just the beginning.

In addition, based on our direct experience, DOL investigations of health plans and health plan service providers are increasingly focused on the structure of plan administrative fees, the descriptions of fees in Administrative Service Agreements, and the ways in which fees are communicated to (and understood by) employers who sponsor self-funded health plans. There is every reason to believe that the DOL will use information gained from these audits as a basis for expanding the scope of the Section 408(b)(2) regulations to cover health and welfare benefit plans.

What to do and where to start?

ERISA provides a “functional” definition of the term fiduciary. Specifically, ERISA defines the term “fiduciary” to include any person who “exercises discretionary authority or control with respect to the management of the plan or plan assets with respect to a plan” or “has discretionary authority or responsibility in the administration of the plan.” This means that a person can be found to be a fiduciary with respect to an employee benefit plan based on the kinds of activities the person engages in, or has the authority to engage in, regardless of the person’s title or other employment duties. Viewed in that light, there is little doubt that an employer that sponsors an ERISA health or welfare benefit plan – and certainly any employer that maintains a self-funded group health plan – will engage in activities of a fiduciary nature with respect to those plans.

One example of such an activity, is the selection of a TPA to administer the plan. The selection of a plan service provider (such as a TPA) is clearly a fiduciary act, the fees paid to a TPA are factored into the premiums paid by employees, and amounts withheld by employers from employee pay to cover their monthly premiums are clearly considered to be plan assets. So, when a small group of HR and finance executives get together to select a TPA to administer their company’s self-funded group health plan, they are engaging in fiduciary act. That act is no different in substance from the act taken by those same executives when they convene a meeting of the company’s 401(k) plan administrative committee to select a recordkeeper for the 401(k) plan. In our view, the process and the governance framework within which these two processes occur should be the same.

With these considerations in mind, we offer the following recommendations to sponsors of welfare benefit plans:

- Determine the fiduciary activities taking place with respect to your health and welfare benefit plans – there will be more than a few;
- Determine who within the management structure of your organization is undertaking these fiduciary activities;
- If fiduciary activities are performed by persons who do not typically have authority to bind your organization to significant legal obligations (sometimes the case with fully insured health and welfare benefits), consider whether it is appropriate or desirable for them to be doing so;

- Form a plan administrative committee made up of appropriate decision makers, analogous to the committee that oversees the administration of (and serves as the legally designated "plan administrator" of) your retirement plans; and
- Have the new committee adopt a charter, keep meeting minutes, use expert consultants, and follow the same basic operating rules as your retirement plan administrative committee.

It has always been the case that a prudent process appropriately documented forms the foundation for good fiduciary compliance. That is as true for ERISA welfare benefit plans as it is for ERISA retirement plans. Now is the time for employers to act accordingly.

Please contact a member of Verrill's Employee Benefits & Executive Compensation Group if you have questions about establishing an administrative committee for your ERISA health and welfare benefit plans.

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