- OneFiduciary Update -

Thursday, October 2, 2008

FIDUCIARY PRUDENCE IS KEY IN TIMES OF MARKET EXTREMES

By: Al Otto, AIFA®

We are experiencing extreme turmoil in the U.S. financial markets. The volatility is incredible, especially compared to the relative low volatility in the markets during the beginning of this decade. While these conditions will have yet-to-be determined effects for plan participants, they certainly amplify the importance of fiduciary prudence for plan fiduciaries.

The Dow Jones Industrial Average was down 777 points on Monday; it was up over 400 points on Tuesday, and closed down slightly the next day. I don't know where it will be at week's end, but there can be little question that the Wall Street that existed at the beginning of this year is no longer the industry that Congress is seeking to rescue from its own excesses. The geography of the U.S. financial world has been permanently altered by the events of the past several weeks. These events were the culmination of a marketplace that evolved over at least two decades. Now Congress is trying to design a rescue plan for a new order whose shape is shifting and frankly a moving target. It is a challenging situation for our leaders and that means it is a challenging situation for every fiduciary of a qualified retirement plan in this country.

There are key considerations for a fiduciary to address in times like these. The first is to stick to the basics: Review your Investment Policy Statement and any other governance protocols; consider the time horizon of your plan(s); focus on your plan participants; help them understand the current situation and not to panic, and lastly document, document, document the process.

Many 401(k) plan fiduciaries are fielding calls from participants who are worried about the future of investment options available to them. It is true that fiduciaries have considerable protection under Section 404(c) of ERISA from claims arising out of participants' investment losses. More important though is the position that the Department of Labor has long taken; if the plan's fiduciaries have imprudently selected the funds from which participants may choose, the 404(c) shield is unavailable. Proper fund selection and ongoing monitoring are a critical component of fiduciary duty.

ERISA requires prudent action, and a fiduciary must act for the interest of the plan participants and their beneficiaries in light of "the circumstances then prevailing." Basically this means that a fiduciary must take current conditions into account. It does not mean that one should abandon the investment policy statement or any of the investment strategies associated with retirement plans. However, if a fiduciary's conduct is ever questioned, a documented process that demonstrates that they considered the effect of current conditions, fiduciary duty and existing strategies would be prudent.

John Mauldin, in his "Outside the Box" introduction on Monday states: "...we will get through this, one way or another. Sanity and clarity will return, as it always does after times of crisis." Mr. Mauldin is right and it is important to keep this in mind when the massive PR machine that we call the media generates the frothy environment that it has. More insight from John Mauldin can be found in our Economic News section at the OneFiduciary website.

Four Clear Strategies for Prudent Action:
Here are some suggested strategies a fiduciary should consider:

1. Poll Plan Fiduciaries and consider calling a special meeting to evaluate the effect of current situation on the plan. Waiting until the next regularly scheduled review meeting might not be considered prudent in light of current volatile market conditions. Even if the fiduciaries decide that no immediate action is necessary, document the discussion and the decision to demonstrate prudence in light of current circumstances.

2. Plan Fiduciaries should ask their service provider and plan advisor for a specific assessment of the implications on their plan's investments.

3. Plan Fiduciaries should ask their service provider or plan advisor for written assessment or re-assurance regarding the financial strength of specific investment options such as Stable Value or Money Market Funds.

4. Communication with participants and beneficiaries is also critical. The purpose is twofold:

a. Communication demonstrates to participants that the fiduciaries are paying attention and also creates a written record of compliance with ERISA.

b. This is an excellent time to re-educate your participants on fundamentally sound long term investment strategies such as the value of asset allocation, risk assessment, buy & hold and dollar cost averaging. Your service provider or investment advisor should have or be able to create collateral to this effect which could be delivered to each participant.

If you would like additional information about these topics or the value of an Independent, Fee-Only Investment Advisor / Retirement Plan Consultant, please visit our website www.onefiduciary.com or send us an e-mail directly.

Al Otto, AIFA®
Chief Executive Officer
al.otto@onefiduciary.com

Brad Larsen, CRPS, AIF®, PRP
Director of Sales & Marketing
b.larsen@onefiduciary.com

(888) 382-8010