

LEGAL UPDATE

Investment Policy Statement

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Clients will occasionally ask whether an investment policy statement (IPS) is a required document under ERISA. The technical answer to the question is clear.

The DOL has never taken the position that it is a required document, and Courts have generally concurred that ERISA does not impose a fiduciary duty to create an IPS. *See*, for

example, *Taylor v. United Technologies* (D. Conn. 2009). (An outlier to this general rule is *Liss v. Smith* (S.D.N.Y. 1998), in which the District Court held, under the facts of that case, that failure to have an IPS was a breach of fiduciary duty.) At the same time, there is widespread agreement that having an investment policy statement is a best practice under ERISA and the overwhelming majority of 401(k) plan sponsors have an IPS in place. If for no other reason than the practical one that if the DOL audits a plan, one of the first documents that it will request will be the plan's IPS. Such activity is consistent with the DOL's view, stated in Interpretive Bulletin 2016-01, that "the maintenance by a plan of an IPS to further the purposes of the plan and its funding policy is consistent with the fiduciary obligations under ERISA Section 404(a)(1)(A) and (B). In addition, because the terms of the statement are an exercise of fiduciary responsibility, an investment policy statement for a plan may need to take into account its funding policy and liquidity needs, as well as issues of prudence, diversification, and other fiduciary requirements of ERISA."

Since it is not a legally required document, the DOL cannot impose a fine or penalty for its absence, but it is an inauspicious manner in which to commence an audit. A second equally important reason for adopting an IPS is that a court, in determining whether there has been a breach of fiduciary duty in connection with an investment decision, will look to the process by which the decision was made. While there is no uniform checklist of activities that a prudent fiduciary must perform, having an IPS in place can be a useful document to provide in this context with the caveat that since an IPS will be treated as one of the documents under which a plan is operated, failure to follow its terms can itself give rise to a breach of fiduciary duty under ERISA. Focusing upon other advantages of an IPS, it allows the relevant plan fiduciaries to have a framework within which to make decisions; provides a guide to the selection, monitoring and

termination of investment decisions; provides for consistency in treatment as the composition of the relevant plan committee changes over time; and clearly sets forth the roles played by various parties involved in the process. Other items that are frequently addressed in an IPS are ERISA Section 404(c) compliance; participant education; asset classes and benchmarking; whether white labeling of funds is appropriate; proxy voting; ESG guidelines; and the prohibition of certain investments, for example, investments generating unrelated business taxable income.

In light of recent discussions concerning the extent to which a relevant plan fiduciary can provide guidance to an investment manager within the context of an ERISA Section 3(38) arrangement, it is interesting to consider the extent to which an applicable fiduciary can exercise control over an investment manager through an IPS (assuming, of course, that the primary draftsman of the IPS was other than the plan's investment manager). The DOL has indicated that a named fiduciary that appoints an investment manager may expressly require, as a condition of the investment management agreement, that the investment manager comply with the terms of the IPS which set forth guidelines on the investments that the investment manager is authorized or not authorized to make. Because the IPS is one of the documents and instruments under which the plan is operated, the investment manager would be required to comply with the IPS insofar as the policy directives or guidelines are consistent with ERISA. Since there are no guidelines as to the permissible level of detail in an IPS, an IPS could be one way in which a named fiduciary could exercise a level of control over the investment strategy of an investment manager.

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