



The Role of the Plan Trustee

Plan sponsors need to understand how plan trusteeship fits within their overall responsibilities.

By Ian Kopelman

Many plan sponsors incorrectly equate the hiring of a trustee with outsourcing their fiduciary duties and potential liability. Such plan sponsors think their involvement ends with establishing the plan and making regular contributions. It can be a rude awakening when plan sponsors discover that, under ERISA, adopting the plan and hiring the trustee is just the beginning of their responsibility.

Understanding the role of the plan's trustee is the plan sponsor's best defense against expensive confusion and errors in plan administration and, even worse, lawsuits by participants or the Department of Labor for fiduciary breaches. The following is a crash course on ERISA's fiduciary rules that outline the roles of the plan administrator or named fiduciary (usually the plan sponsor) and the trustees.

1 The trustee is not the only fiduciary under ERISA.

ERISA defines a plan fiduciary as any of the following: the trustee, the named fiduciary for the plan, the plan administrator, the investment manager, and anyone else to the extent that person exercises any discretionary authority or control in the management of the plan or disposition of plan assets, can or does render investment advice for a fee, or has any discretionary authority or control in administering the plan. The

test for fiduciary status is purely functional. Anyone from the chief executive officer to a human resources assistant could be in a position to exercise "any discretionary authority" with respect to plan assets and plan administration and only discover later that he or she is an ERISA fiduciary with all the potential liability that entails.

2 Every plan has a named fiduciary and plan administrator and they are usually the plan sponsor.

The named fiduciary for the plan must be identified in the plan document or designated under procedures set out in the plan document. It may be a separate entity such as the trustee, an individual, a position designated by title, a committee, or the plan sponsor. Under most prototype and standardized plan and trust documents, the plan sponsor, one of its officers, or a committee of its employees is designated as the named fiduciary. As with the named fiduciary, the plan administrator is usually named in the plan document (and is usually the plan sponsor). If the plan document does not designate the plan administrator, under ERISA it is presumed to be the plan sponsor. As plan administrator, the plan sponsor is responsible for plan design and interpretation, investment of plan assets, and operation of the plan. The plan administrator remains responsible for the proper execution of each of these

responsibilities, even if they are actually discharged by an outside vendor.

3 A trustee is one kind of fiduciary — but there are two kinds of trustees.

ERISA section 403(a) requires that all plan assets (other than insurance contracts) be held in trust by a trustee named in the plan or trust document or appointed by a named fiduciary identified in the plan document. It also provides that the trustee has exclusive authority and discretion to manage and control the assets of the plan, except to the extent that the plan expressly provides that the trustee is subject to the direction of the named fiduciary (who is not the trustee) or that authority over plan assets is delegated to an investment manager. As a result, trustees under ERISA can be divided into two separate categories: discretionary trustees and directed trustees.

4 A discretionary trustee is what the plan sponsor thinks it hired.

Discretionary trustees typically have complete responsibility for the assets of the plan, including the selection and monitoring of investments, selection and performance of service providers, proper distribution of assets, and because of ERISA's co-fiduciary liability rules, proper plan administration. This is the role most commonly assigned to

trustees in personal trusts and is the role most plan sponsors have in mind when they hire a trustee.

5 A directed trustee does what it is told.

The directed trustee is the most common type of trustee for ERISA plan assets and is the role assigned to the trustee under most prototype and other standardized plan and trust documents. A directed trustee is subject to the direction of the named fiduciary of



the plan or some entity appointed by the named fiduciary. It has no discretionary authority with respect to the investment of plan assets, selection of service providers, distribution of assets, or proper plan administration and acts more like a custodian than a discretionary trustee. While Enron and similar litigation may have called into question the extent to which a directed trustee is absolved of responsibility, it has not erased the distinction between the two types of trustees

The responsibilities delegated to the directed trustee are generally laid out in the plan and trust documents. In a prototype or standardized plan document, these responsibilities may be very narrow and non-negotiable. With a custom plan and trust, the plan spon-

sor and the trustee negotiate the nature of the trustee's duties and responsibilities under ERISA before the agreement is signed.

Regardless of the nature of the document, a directed trustee will almost always be responsible for:

- Custody and safekeeping of the plan's assets;
- Proper execution of directions from the named fiduciary, plan administrator, and investment manager; and
- Trust accounting

6 The named fiduciary can run but it can't hide.

To put it more accurately, the named fiduciary of a plan can delegate, but not escape its fiduciary responsibilities under ERISA. The named fiduciary has authority to control and manage the operation and administration of the plan. While it may delegate fiduciary functions to a trustee, plan administrator, or investment manager, the named fiduciary retains ultimate fiduciary responsibility for its choices and must comply with ERISA's requirement in selecting other plan fiduciaries and delegating its duties.

Complying with ERISA's requirements means that selection of another fiduciary must be:

- For the exclusive benefit of plan participants and their beneficiaries and for the purpose of defraying expenses of administering the plan;
- Prudent, which means that it must be done with the care, skill, and diligence that would be exercised by a reasonably prudent person who is familiar with such matters; and
- In accordance with the plan documents, unless the documents themselves are not in compliance with the terms of ERISA.

However, the named fiduciary's work does not end with the selection of other fiduciaries in accordance with the above requirements. It always retains a duty to monitor the performance of the

other fiduciaries on an ongoing basis and prevent or correct any breaches of duty by the fiduciaries.

7 The basic fiduciary rules always apply.

The exclusive benefit, prudence, and compliance requirements discussed so far apply to all actions of the named fiduciary and plan administrator, including the following:

- Appointing the trustee;
- Appointing investment managers;
- Investing plan assets;
- Selecting plan service providers; and
- Monitoring the performance of all of the above on an ongoing basis

As a result, it is not enough just to select a trustee, an investment manager, or non-fiduciary service provider; the selection must be prudent, for the exclusive benefit of the plan participants and their beneficiaries, and in compliance with the terms of the plan and of ERISA.

8 The plan sponsor, whether acting as named fiduciary or plan administrator, can follow the rules and still be on the hook.

Because of ERISA's rules regarding co-fiduciary liability, a named fiduciary can act in good faith and comply with all the requirements described above, and still be financially liable for another fiduciary's breach. ERISA section 405 imposes liability for the acts and omissions of a co-fiduciary in the following circumstances:

- If the fiduciary knows that the person committing the act or omission is a fiduciary with respect to the same plan, participates knowingly in the act or omission, and knows that the act or omission is a breach of fiduciary duty;
- If the fiduciary's breach of ERISA's rules enabled the subsequent breach by a co-fiduciary; and

- If the fiduciary knows of a breach by a co-fiduciary and fails to make reasonable efforts under the circumstances to remedy the breach.

Section 405 of ERISA also provides that any fiduciary that breaches his or her fiduciary duty is personally liable for any breach of responsibility with respect to a plan. This can include an obligation to make good any losses suffered by the plan as a result of the breach. Action to enforce these rules may be brought by the Department of Labor or by any participant on behalf of the plan.

9 Don't forget the paperwork.

The best defense any fiduciary under ERISA (including a trustee) has against claims that it breached its fiduciary duties is a complete paper trail. For the named fiduciary this means the following:

- Formulating (and periodically reviewing) a formal written investment policy statement;
- Documenting due diligence in the selection of plan fiduciaries and other service providers;
- Periodically auditing the performance of those service providers;
- Looking at the performance and relative expenses of plan investments;
- Getting expert help when necessary;
- Maintaining all information related to the plan and received from the trustee and other service providers;
- Having actual meetings, documented with minutes, if the named fiduciary is a committee;
- Providing service providers (including the directed trustee) with written directions signed by authorized individuals for all actions with respect to the plan; and
- Understanding and complying with ERISA's reporting requirements.

Most importantly, the plan sponsor must accept that as named fiduciary and/or plan administrator, it is ultimately responsible for the plan's compliance with ERISA. Each trustee, investment manager, and recordkeeper knows only its individual part of the story. Only the plan sponsor knows all the parties involved, including the participants. No outside vendor can (or wants to) take the responsibility for making decisions for the named fiduciary. Ultimate fiduciary responsibility for the plan remains with the named fiduciary/plan administrator — usually the plan sponsor. ➤

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