

MEMO# 11948

June 14, 2000

NINTH CIRCUIT CASE HELD THIRD-PARTY ADMINISTRATOR NOT A PLAN FIDUCIARY

[11948] June 14, 2000 TO: PENSION COMMITTEE No. 39-00 RE: NINTH CIRCUIT CASE HELD THIRD-PARTY ADMINISTRATOR NOT A PLAN FIDUCIARY

In CSA 401(k) Plan et al. v. Pension Professionals, Inc. (No. 98-56012), the Ninth Circuit held that a third party administrator of a pension plan that performed solely ministerial functions was not a fiduciary under ERISA and thus did not have a duty to warn plan participants about its suspicion of embezzlement by plan trustees. The facts of the case are as follows. Computer Software Analysts ("CSA") hired Pension Professionals, Inc. ("PPI") to prepare financial reports and to perform other third-party administrative services for its 401(k) plan. The service agreement specified that PPI was to serve as a third-party administrator to the plan and not as a fiduciary. PPI later discovered discrepancies between the amount of funds CSA withheld from employees' paychecks as contributions to the plans and the amounts actually deposited into participants' accounts. PPI suspected embezzlement by a trustee of the plan who also served as chief executive officer of CSA. PPI notified the trustees of the plan that the failure to deposit employees' contributions into their accounts violated Internal Revenue Service and Department of Labor regulations and that the failure could be classified as both embezzlement and as a breach of fiduciary duty under ERISA. The trustees reassured PPI that CSA intended to bring all plan assets current and agreed to a repayment schedule. After consulting with legal counsel, PPI agreed to remain as the CSA plan's third-party administrator as long as the trustees adhered to the repayment schedule. PPI also placed language on all participant account statements stating the following: "Contrary to the requirements of the Department of Labor and the Internal Revenue Service, a portion of the 401(k) benefits has not yet been received by the trust." The trustee later asked PPI to modify the repayment schedule. PPI denied the request and reminded the trustee that it would resign as third-party administrator to the plan if CSA did not honor the repayment schedule. After receiving falsified financial statements from CSA, PPI resigned as third-party administrator to the plan. Upon resigning, PPI did not alert law enforcement authorities or plan participants about its suspicions regarding the trustee's embezzlement of plan assets. A number of former CSA employees and participants in the plan sued PPI, seeking recovery of the embezzled funds and asserting that PPI was liable as a fiduciary under ERISA for the misappropriated plan contributions. The plaintiffs argued that PPI's conditions for continued employment by CSA established effective control over the plan. The court held that PPI's functions were ministerial tasks that did not give rise to fiduciary liability. The court rejected the plaintiffs' claims that PPI gained control over the plan noting that the conditions that PPI imposed, i.e., the repayment schedule, were designed to assert control over its own engagement and not to exercise discretionary authority or control over the plan's management or administration. Finally, the court

rejected the plaintiffs' claims that PPI had a duty to report the suspected embezzlement to the plan participants. Because PPI was not a fiduciary, the court reasoned, it did not have an affirmative duty to warn plan participants of threats to their benefits. A copy of the case is attached. Kathryn A. Ricard Associate Counsel Attachment

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