

**MEMO# 18350**

December 21, 2004

## **DEPARTMENT OF LABOR ISSUES GUIDANCE ON THE RESPONSIBILITIES OF DIRECTED TRUSTEES UNDER ERISA**

[18350] December 21, 2004 TO: PENSION MEMBERS No. 62-04 PENSION OPERATIONS ADVISORY COMMITTEE No. 83-04 RE: DEPARTMENT OF LABOR ISSUES GUIDANCE ON THE RESPONSIBILITIES OF DIRECTED TRUSTEES UNDER ERISA The Department of Labor has issued Field Assistance Bulletin (FAB) 2004-03, which provides general guidance to the Employee Benefits Security Administration's regional offices regarding the Department's views on the responsibilities of directed trustees under section 403(a)(1) of ERISA, particularly with respect to directions involving employer securities.<sup>1</sup> The FAB begins with a discussion of the directed trustee provisions of ERISA. According to the FAB, a plan trustee "will by definition, always be a 'fiduciary' under ERISA as [a] result of its authority or control over plan assets." Section 403(a)(1), which describes trustees that are subject to the direction of a named fiduciary who is not a trustee, significantly limits the directed trustee's responsibilities as a plan fiduciary. Specifically, a directed trustee is subject to the proper directions of the named fiduciary, and a direction is proper only if it is (1) made in accordance with the terms of the plan; and (2) not contrary to ERISA. In Accordance with the Terms of the Plan According to the FAB, a directed trustee may not follow a direction that the trustee knows or should know is inconsistent with the terms of the plan. In order to make such determinations, directed trustees have a duty to request and review all the documents and instruments governing the plan that are relevant to its duties as directed trustee. The Department considers a direction to be consistent with the terms of a plan if the relevant documents do not prohibit the direction. If the directed trustee determines that the plan terms are ambiguous with respect to the permissibility of the direction, then the directed trustee should obtain a clarification of the plan terms from the fiduciary responsible for interpreting such terms. The FAB states that the directed trustee may rely on the interpretation of such fiduciary. <sup>1</sup> The text of the Field Assistance Bulletin is available at: [http://www.dol.gov/ebsa/regs/fab\\_2004-3.html](http://www.dol.gov/ebsa/regs/fab_2004-3.html). <sup>2</sup> Not Contrary to ERISA The FAB states that a directed trustee may not follow a direction that the trustee knows or should know is contrary to ERISA, and provides specific examples concerning ERISA's prohibited transaction provisions and prudence requirement. Prohibited Transactions According to the FAB, a directed trustee must follow processes that are designed to avoid prohibited transactions. In order to satisfy this obligation, the FAB recommends that the directed trustee obtain appropriate written representations from the directing fiduciary that the plan maintains and follows procedures for identifying prohibited transactions. In addition, these procedures should identify the individual or class exemption applicable to the transaction. The directed trustee may rely on these representations unless it knows that the representations are false. Prudence Requirement With respect to the prudence

requirement of section 404(a)(1) of ERISA, the named fiduciary has primary responsibility for determining the prudence of a particular transaction, and the scope of a directed trustee's responsibility is significantly limited. The FAB states that a directed trustee (1) does not have an independent obligation to determine the prudence of every transaction; and (2) does not have an obligation to duplicate or second-guess the work of the plan fiduciaries that have discretionary authority over the management of plan assets. The primary circumstance in which an obligation to question market transactions involving public traded stock could arise, according to the FAB, is when the directed trustee possesses material non-public information regarding a security. In this situation, the directed trustee, prior to following a direction that would be affected by such information, has a duty to inquire about the named fiduciary's knowledge and consideration of the information with respect to the direction.<sup>2</sup> Similarly, if the directed trustee performed an internal analysis in which it concluded that the company's current financial statements were materially inaccurate, the directed trustee would have the responsibility to disclose this information to the named fiduciary before making a determination whether to follow a direction to purchase the company's stock. Absent material non-public information, the directed trustee will rarely have an obligation under ERISA to question the prudence of a direction to purchase publicly traded securities at the market price solely on the basis of publicly available information. According to the FAB, even a steep drop in a stock's price would not, in and of itself, indicate that a named fiduciary's direction to purchase or hold such stock was imprudent and, therefore, not a proper direction. In limited, extraordinary circumstances, where there are clear and compelling public indicators, as evidenced by an SEC Form 8-K filing,<sup>3</sup> a bankruptcy filing or similar public indicator, that call into serious question a company's viability as a going concern, the directed trustee may have a duty not to follow the named fiduciary's instruction without further inquiry. This duty would not be triggered, however, by mere media speculation as to the continued viability of the company, or the bare fact that a regulatory body has opened an investigation of the company. Consequences of Questioning Directions Finally, the FAB states that neither a directed trustee's questioning of the proper nature of directions nor its declining to follow a direction will change the nature and scope of a directed trustee's fiduciary responsibility. For example, information provided to a named fiduciary regarding the prudence of an investment is not "investment advice" for purposes of ERISA. Also, the directed trustee remains "directed" even if the named fiduciary changes a direction in response to the directed trustee's inquiries or information.<sup>4</sup> Kathy D. Ireland Senior Associate Counsel

<sup>3</sup> A footnote to the FAB adds that the SEC recently expanded the number of reportable events triggering a Form 8-K filing obligation, and notes that only those relatively few Form 8-K's that call into serious question a company's ongoing viability may trigger a duty on the part of the directed trustee to take some action.

<sup>4</sup> The FAB also addresses co-fiduciary liability under section 405(a)(1) of ERISA, noting that the directed trustee may be liable if it knowingly participates in the breach of another fiduciary, unless the directed trustee takes reasonable steps to remedy the breach. Examples of such steps include reporting the breach to other plan fiduciaries or to the Department of Labor.