U.S. Department of Labor

Labor-Management Services Administration
Washington, D.C. 20216

Reply to the Attention of:

OPINION NO. 82-62A
Sec. 408(b)(2)

DEC 8 1982

Identification Number: F-2411A

Gentlemen:

This is in response to your letter of June 1, 1982, enclosing a request for an advisory opinion concerning the application of the prohibited transactions provisions of section 406 of the Employee Retirement Income Security Act of 1974 (ERISA) and section 4975 of the Internal Revenue Code of 1954 (the Code) to the retention by the (Company) of its lower tier subsidiary, (Bank) to serve as trustee of certain employee benefit plans maintained by (Company) and members of its controlled group (as defined under sections 414(b) and (c) of the Code).

You represent that (Company) and other members of its controlled group maintain several employee benefit plans which are either qualified under section 401(a) of the Code or tax exempt welfare plans under section 501(a) of the Code. It is presently contemplated that the assets of certain of these employee benefit plans (the Plans) will be transferred to (Bank), a subsidiary of (Company) which participates in the consolidated Federal income tax return filed by (Company). (Bank) will establish separate and distinct trusts for the assets of each of those employee benefit plans. Several of the plans will also participate in a master trust which (Bank) will establish for plans maintained by (Company) and its controlled group. Thus, (Bank) will serve in both individual and master trustee capacities.

You represent that (Bank) will be both a party in interest and a fiduciary with respect to the Plans. (Bank's) fees will be paid by (Company) and members of its controlled group and will be at the same rate charged by (Bank) to unrelated customers for similar services.

(Bank) will not have investment discretion over plan assets held in either the master or individual trusts. It will perform services equivalent to a directed trustee or custodian. The (the Committee), comprised of senior executives of (Company), selected (Bank) to provide trustee services after consideration was give to the services provided by other institutions. The Committee has investment discretion over a portion of the assets of the Plans with the majority of the assets being invested by professional managers that are unrelated to (Company). Instructions may be

given to (Bank) to invest plan assets in its commingled short-term investment fund or that any assets for which investment instructions have not been received shall be invested in that fund pending the receipt of further instructions. Fees charged for investment in (Bank's) short-term investment fund are encompassed in (Bank's) trustees fees and are paid directly by (Company). (Bank) does not charge a transaction fee to its pension fund clients for the investment in or withdrawal of funds from its short-term investment fund, nor does (Bank) retain a percentage of earnings of its short-term investment fund. You state that the Committee has the discretion to replace (Bank) on reasonably short notice without penalty to the Plans.

You request an advisory opinion under section 406 of ERISA that (Company) and other members of its controlled group may retain (Bank) as trustee of various employee benefit plans which (Company) or any member of its controlled group maintain, or in the future may maintain, and that (Bank) may be paid reasonable compensation for trustee service performed. In addition, you seek an opinion that plan assets may be invested in (Bank's) commingled short-term investment fund without engaging in a prohibited transaction under section 406 of ERISA.

Under Reorganization Plan No. 4 of 1978 (43 FR 47713, October 17, 1978), the authority of the Secretary of the Treasury to issue rulings under section 4975 of the Code has been transferred, with certain exceptions not here relevant, to the Secretary of Labor. Therefore, the references in this letter to specific sections of ERISA refer also to the corresponding sections of the Code.

Section 406(a)(1)(C) and (D) of ERISA prohibit a fiduciary with respect to a plan from causing the plan to engage in a transaction which the fiduciary knows or should know constitutes a direct or indirect furnishing of goods, services or facilities between the plan and a party in interest or results in a transfer to, or use by or for the benefit of, a party in interest, of any assets of the plan. Section 406(b)(1) and (2) of ERISA provide that a fiduciary with respect to a plan shall not (1) deal with the assets of the plan in his or her own interest or for his or her own account, or (2) in his or her individual or in any other capacity act in any transaction involving the plan on behalf of a party (or represent a party) whose interests are adverse to the interests of the plan or the interests of its participants or beneficiaries.

(Bank) is a party in interest with respect to the Plans under section 3(14) of ERISA because of its relationship to (Company) and would be a fiduciary under section 3(21) of ERISA upon its appointment as trustee. The Committee is a fiduciary under ERISA section 3(21) by reason of its discretionary authority in the administration of the Plans and is, therefore, a party in interest with respect to those Plans under section 3(14)(A). Accordingly, the prohibited transactions provisions of section 406 of ERISA described above would apply to transactions involving (Bank) in the absence of a statutory or administrative exemption.

Section 408(b)(2) of ERISA exempts from the prohibitions of section 406(a) any contract or reasonable arrangement with a party in interest, including a fiduciary, for office space, or legal, accounting or other services necessary for the establishment or operation of the plan, if no more than reasonable compensation is paid therefor. Section 408(c)(2) of ERISA provides, in relevant

part, that nothing in section 406 shall be construed to prohibit any fiduciary from receiving compensation for services rendered, or for the reimbursement of expenses properly and actually incurred, in the performance of his or her duties with respect to the plan. Regulations issued by the Department clarify the terms "necessary service" (29 CFR §2550.408b-2(b)), "reasonable contract or arrangement" (29 CFR §2550.408b-2(c)) and "reasonable compensation" (29 CFR §§2550.408b2(d) and 2550.408c-2) as used in sections 408(b)(2) and 408(c)(2) of ERISA.

Section 408(b)(8) of ERISA further provides, in pertinent part, that section 406(a)(1) of ERISA does not apply to any transaction between a plan and a common or collective trust fund maintained by a bank or trust company supervised by a State or Federal agency, if (a) the transaction is a sale or purchase of an interest in the fund, (b) the bank or trust company receives not more than reasonable compensation, and (c) the transaction is expressly permitted by the instrument under which the plan is maintained, or by a fiduciary (other than the bank or trust company or an affiliate thereof) who has authority to manage and control the assets of the plan.

The provision of trustee services by (Bank) to the Plans and the investment of Plan funds in (Bank's) commingled short-term investment fund would be exempt from the prohibitions of section 406(a) of ERISA provided that the conditions of sections 408(b)(2) and 408(b)(8), respectively, are met. Whether the conditions are met in each case involves questions which are inherently factual in nature. Section 5.01 of ERISA Advisory Opinion Procedure 76-1 (ERISA Proc. 76-1, 41 FR 36281, August 27, 1976) states that the Department generally will not issue opinions on such questions. The trustees of the Plans, or other appropriate plan fiduciaries, must determine, based on all the relevant facts and circumstances, whether the conditions of sections 408(b)(2) and 408(b)(8) are satisfied.

With respect to the prohibitions in section 406(b), regulation 29 CFR §2550.408b-2(a) indicates that section 408(b)(2) of ERISA does not contain an exemption for an act described in section 406(b) of ERISA even if such act occurs in connection with a provision of services which is exempt under section 408(b)(2). As explained in regulation 29 CFR §2550.408b-2(e)(1), if a fiduciary uses the authority, control or responsibility which makes him or her a fiduciary to cause the plan to enter into a transaction involving the provision of services when such fiduciary has an interest in the transaction which may affect the exercise of his or her best judgement as a fiduciary, a transaction described in section 406(b) of ERISA would occur, and that transaction would be deemed to be a separate transaction from the transaction involving the provision of services and would not be exempted by section 408(b)(2) of ERISA.

The mere selection of (Bank) to provide trustee services to the Plans would not, in itself, constitute a violation of ERISA section 406(b)(1). However, because a violation of the self-dealing proscription contained in section 406(b)(1) could occur in the course of the Committee's deliberations regarding the retention of (Bank) as trustee, the Department is unable to rule that the decision to retain (Bank) would never violate that section.

It is the Department's view that generally a fiduciary's decision to retain a service provider whose fees will be paid by the plan sponsors will not involve an adversity of interests as contemplated by section 406(b)(2) of ERISA. However, if, under the particular facts and circumstances, a fiduciary of the plan is in a position to benefit, or to cause a person to whom the fiduciary has an interest to benefit, from such a decision at the expense of the plan, the decision to retain the service provider would result in a violation of section 406(b)(2) of ERISA. Accordingly, the Committee's decision to retain (Bank) to provide trustee or custodial services to the Plans would not, in itself, constitute a violation of section 406(b)(2).

In the absence of regulations, the Department is not prepared at this time to indicate the extent, if any, to which section 408(b)(8) applies to the prohibitions under section 406(b) of ERISA. See Proposed Class Exemption for Certain Transactions Involving Bank Collective Funds, 44 FR 44290, 44291 n.3, July 27, 1979. If, however, (Bank) does not exercise any authority, control or responsibility that would make it a fiduciary to cause the assets of the Plans to be invested in its commingled short-term investment fund, it does not appear that the investment of the Plans' assets in that fund would involve (Bank) in acts described in section 406(b)(1) of ERISA.

This letter is an advisory opinion under ERISA Proc. 76-1. Section 10 of the procedure explains the effect of advisory opinions.

Sincerely,

Alan D. Lebowitz
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Pension and Welfare Benefit Programs