U.S. Department of Labor

Pension and Welfare Benefits Administration
Washington, D.C. 20210

SEP 13, 1993

93-24A
ERISA SEC.
406(b)(1), 406(b)(3)

Roger W. Thomas
Staff Attorney
Department of Financial Institutions
Fourth Floor, The John Sevier Building
500 Charlotte Avenue
Nashville, TN 37243-0705

Dear Mr. Thomas:

This is in response to your inquiry whether certain transactions engaged in by a Tennessee bank are consistent with the Employee Retirement Income Security Act of 1974 (ERISA). In particular, you call attention to an asserted "common industry practice" whereby banks acting as agents or trustees for employee benefit plans earn interest for their own accounts from the "float" when a benefit check is written to a participant until the check is presented for payment.

You indicate that a company (Trust Company), which is chartered under Tennessee law as a non-depository bank limited to trust powers, acts as an agent or trustee for various employee benefit plans. It also offers various collective investment funds in which plans invest. A national bank (National Bank) located in Tennessee serves as custodian for some of these plans.

In connection with the administration of the plans, Trust Company maintains accounts at National Bank, including a "General Account" and a "Disbursement Account." When Trust Company is directed to liquidate pooled fund assets to pay benefits, unless it is specifically directed to wire the funds to the participant, it transfers the funds to the General Account and simultaneously issues a check payable to the participant from the Disbursement Account. When checks are presented for payment, funds are wired from the General to the Disbursement Account. In the interim, Trust Company earns income on such funds for its own account, pursuant to a retail repurchase agreement with National Bank.

You question whether the payment of this income to Trust Company is a prohibited receipt by a fiduciary of consideration from a party dealing with the plan in connection with a transaction involving the assets of the plan under section 406(b)(3) of ERISA. You also express concern that the Trust Company may be violating ERISA by dealing with National Bank, given National Bank's relationship to the plans.

Trust Company, through its attorney, contends that once a check is written to a participant, corresponding amounts in the General Account cease to be plan assets. In support of this argument Trust Company relies upon the first example of the participant contribution regulation in 29 C.F.R. 2510.3-102, which addresses when amounts that an employer withholds from a participant's pay for contribution to a plan can reasonably be segregated from the employer's general assets, and thus become assets of the plan for certain purposes. These special rules concerning segregation of participant contributions from an employer's general assets, however, have no application to the question of whether a plan has an interest in an administrative account when plan assets are transferred to the account in support of an outstanding benefit check.[1]

Turning to an analysis of the issues presented, section 406(b)(1) of ERISA states that a fiduciary with respect to a plan shall not deal with the assets of the plan in his or her own interest or for his or her own account. Section 3(21)(A) of ERISA defines a fiduciary, in part, as one who exercises any discretionary authority with respect to the assets of a plan. As explained in 29 C.F.R. 2509.75-8, persons serving as plan trustees (and certain other plan officials) will be fiduciaries due to the very nature of their positions. Other persons will be fiduciaries to the extent that they perform any of the functions described in section 3(21)(A) of ERISA.

Accordingly, it is the view of the Department that, based on the facts described above, where a fiduciary (e.g. Trust Company) exercises discretion with regard to plan assets, its receipt of income from the "float" on benefit checks under a repurchase agreement with a national bank in connection with the investment of such plan assets would result in a transaction described in ERISA section 406(b)(1).[2]

Moreover, even if all income earned under the repurchase agreements were allocated to the plans, the repurchase agreements themselves may be prohibited where the national bank is a party in interest with respect to the plans. Section 406(a)(1)(A) and (B) of ERISA, in part, prohibit sales or extensions of credit between plans and parties in interest. The term "party in interest" is defined in section 3(14) of ERISA to include a person providing services to a plan. From the information provided, it appears that National Bank, as the custodian of plan assets for some of the plans, is a service provider to such plans.

As we understand it, repurchase agreements essentially involve debt transactions structured as sales of securities. Therefore, absent exemptive relief, it appears that the repurchase agreements in question would involve prohibited extensions of credit, as well as prohibited sales between National Bank and plans that it serves. The Department has issued an administrative exemption, Prohibited Transaction Exemption 81-8 (copy enclosed), which provides conditional relief for investments in repurchase agreements, by or on behalf of an employee benefit plan. Whether this class exemption would grant relief to the parties involved in the subject retail repurchase agreement cannot be determined from the information provided.

This letter constitutes an advisory opinion under ERISA Procedure 76-1 Accordingly, it is issued subject to the provisions of that procedure, including section 10 thereof relating to the effect of advisory opinions.

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[1] It is commonly understood that a check does not of itself operate as an assignment of any funds in the hands of the drawee bank available for its payment and the bank is not liable on the instrument until it accepts it. U.C.C. §3-409(1). A bank which properly pays checks drawn on it extinguishes its liability to the depositor to the extent of the amount so paid, so that it may charge the depositor's account with the amount of such payment. 9 C.J.S. Banks and Banking § 353 (1938).

[2] Although you asked if this arrangement would be prohibited under section 406(b)(3), due to the limited information provided we are unable to conclude that the arrangement described herein gives rise to a violation of this section. Specifically, we are unable to conclude that the bank knew, or should have known, the circumstances under which plan assets were invested pursuant to the repurchase agreements. Thus, we are restricting our analysis to the potential violation of section 406(b)(1).

Sincerely,

Robert J. Doyle
Director of Regulations and Interpretations

Enclosure