

# Discretionary vs. Directed Trustee



RETIREMENT MANAGEMENT SERVICES, LLC  
*Plan Consulting • Administration • Design*

## Discretionary vs. Directed Trustee



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Over the next few months, retirement plan sponsors will be amending and restating plan documents for the Pension Protection Act (PPA). *All volume submitter and prototype plan documents are required to be restated for PPA no later than April 30, 2016.*

During the restatement process, the retirement plan committee or Plan Administrator should review current plan provisions for any design changes they want to make as the plan is updated. One important consideration for plan design is the designation of the plan's trustee(s). A **Plan Trustee** is responsible for maintaining and managing plan assets. The trustee can process contributions, disbursements and other transactions and issue statements or he can delegate these tasks to a third party. We are often asked who can be a trustee, what are the trustee's responsibilities and liabilities, and if naming an outside trust company as trustee removes liability from company officials.

A trustee can be an individual(s) or an institution. Some employers choose to "self-trustee" the plan. This means that the Plan Sponsor has named certain employees of the company or a plan committee as the trustee. The plan document will specifically name the trustee(s) and will contain trust language that explains the investment powers and responsibilities of the trustee. If an institutional trust company is named as plan trustee, then the plan document will contain language indicating that the trustee's powers are determined under a separate trust agreement which replaces or is adopted in conjunction with the trust language written in the plan document.

Regardless of whether the plan is self-trusteed or uses an outside trust service, the trust document will further describe whether the named trustees are **Nondiscretionary (or Directed) Trustees or Discretionary Trustees**. Although a plan trustee is always a "fiduciary" as result of its authority or control over plan assets, a Directed Trustee assumes less responsibility and less liability because it is basically just following the investment directions given to it by the plan sponsor, investment manager or plan participants. The duties of a Directed Trustee are therefore significantly narrower than the duties of a Discretionary Trustee. A Discretionary Trustee is held to a higher standard of care than a Directed Trustee.



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## DIRECTED TRUSTEES

A Directed Trustee is only considered a plan fiduciary to the extent that it is making discretionary decisions about the plan assets. Most Directed Trustees do not give investment advice and do not make any discretionary investment decisions. If the Directed Trustee is simply processing the investment directions given to it by others, the DOL (Department of Labor) defines the role of directed trustees to the investment of plan assets as follows:

- Person(s) providing direction to the trustee must be authorized under the plan document.
- The trustee must review the plan document, trust document, Investment Policy Statement and all other documents governing the plan to determine its role and liability. Any ambiguous details need to be clarified.
- The direction given to the trustee must not be contrary to ERISA. (The Employee Retirement Income Security Act of 1974 was established to govern the rights of participants, beneficiaries and the obligations of plan fiduciaries. It also encompasses IRS and DOL regulations.)

Recent court cases have clarified that a Directed Trustee does not have a direct obligation of prudence under ERISA and is not required to second-guess the investment instructions given to it. The Directed Trustee must simply make sure that the directions it has been given are proper and in accordance with plan terms. If the Directed Trustee knows that the investment direction given is not consistent with the plan terms or violates ERISA, the Directed Trustee may not follow the direction.



Directed Trustees can take certain steps to be protected from liability for investment decision making:

- Review plan documents and signature cards to confirm those signing are authorized.
- Review investment policies or other documentation that may limit investment options.
- Review investment procedures to ensure no prohibited transactions occur.
- Monitor public information regarding bankruptcy, charges brought against company representatives or 8-K filings (Form completed by public companies for the Securities and Exchange Commission reporting major events shareholders should know about).
- Review insurance coverage, other protection and fees to ensure risks are adequately covered. A fidelity bond is required for all persons handling plan assets. A fidelity bond protects against losses due to fraud or dishonesty, i.e. theft, embezzlement or forgery. For protection against losses not due to fraud or dishonesty, fiduciary liability insurance should be purchased.

It is common for plans that are self-trusted to specifically note that the named trustees are Directed Trustees only. If the plan provides for participant direction of assets, then as long as certain disclosure and procedural requirements are met, the Directed Trustee will not be held liable for any losses that a participant incurs to his account.

### **DISCRETIONARY TRUSTEES**

Discretionary Trustees may direct plan assets at their own discretion, unless they are given specific investment direction by the Plan Administrator, named Fiduciary, Investment Manager or plan participants. The Discretionary Trustee may be an employee of the company, but it is more likely that this role will be outsourced to a third party investment manager or corporate trustee. Using an outside corporate trustee does add a layer of protection for the Plan Administrator by distributing fiduciary responsibility more broadly. When considering the use of an outside Discretionary Trustee, the Plan Administrator will need to understand the fees associated with that service and, if those fees are being charged to the plan, ensure that the fees are reasonable for the service. If the plan is self-trusted and the named trustee is a Discretionary Trustee, the management of plan assets may still be delegated to an outside investment manager and the trustee will not have fiduciary liability with respect to assets under the control of the investment manager but retains liability for monitoring the suitability and performance of the outside investment manager.

The appointment of the plan trustee is an important decision that must be understood and carefully considered by the Plan Administrator or retirement plan committee. It is wise to discuss this decision with your investment provider and third party administrator before naming the trustee in the plan document. The choice of plan trustee will be largely dependent on whether the plan allows for participant directed accounts and whether the Plan Administrator feels that paying an outside trust company transfers enough liability for investment decision making sufficient to warrant the annual fee charged by the trust company.



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