Trustee and Plan Expense Issues

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Updated November 2006

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Questions and Answers

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August 2004
Updated August 2005
Updated November 2006

Introduction

During the many years in which we have advised clients on fiduciary matters, it has become apparent that questions related to appropriate trustee and plan expenses sometimes cause confusion for plan fiduciaries and their advisors. In part, this problem is due to the lack of definitive or comprehensive guidance from the U.S. Department of Labor (DOL), the Federal agency that is charged with administering and enforcing the fiduciary rules under the Employee Retirement Income Security Act of 1974 (ERISA). But perhaps more importantly, even if the agency were inclined to issue definitive guidance on these issues, it would be difficult to do so because the application of ERISA's fiduciary principles is based on the individual facts and circumstances of each situation, including the extent to which decisions regarding trustee and plan expenses have been documented by plan fiduciaries. This makes definitive, generally applicable guidance extremely hard to fashion.

Nevertheless, we believe it may be useful for plan fiduciaries and their advisors to have access in a single place to information collected from a variety of sources that illustrates the range of opinions that have been expressed by the DOL regarding questions relating to trustee and plan expenses.

However, we caution readers of this paper that the compilation of information we present here does not constitute definitive guidance as to what the law is regarding these questions. As previously noted, definitive guidance is impossible since the facts and circumstances of an individual case, including the documentation process, are critical to whether DOL chooses to find and pursue a violation. In fact, in compiling this information, we have found significant differences in the way in which DOL has treated certain issues. Certainly most of this is due to the underlying circumstances but some is also due to differences among individual investigators, different regional offices of DOL and between the field offices and DOL National Office.

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[1] We gratefully acknowledge the contributions of our colleagues who have provided us with their ideas and experiences: Larry R. Beebe, CPA, Bond, Beebe; Ellen O. Boardman, O'Donoghue & O'Donoghue, LLP; Phyllis C. Borzi, O'Donoghue & O'Donoghue LLP; Richard Calcara, Blake and Uhlig, P.A.; Donald J. Capuano, O'Donoghue & O'Donoghue LLP; James V. Cole, II, The Groom Law Group; Randy DeFrehn, National Coordinating Committee for Multiemployer Plans; William K. Ecklund, Felhaber, Larson, Fenlon & Vogt; Michael Fanning, International Union of Operating Engineers Central Pension Fund; William Halbert, International Brotherhood of Carpenters & Joiners of America, AFL-CIO; Nancy Juda, Lerach Coughlin Stoia Geller Rudman & Robbins, L.L.P.; William Lurye, Robein, Urann & Lurye; Judy Mazo, The Segal Company; Peter Novak, CPA, Novak Francella L.L.C.; Robert M. Projansky, Proskauer Rose L.L.P.; Patrick Riley, Counsel Sheet Metal Workers' International Association;; Jeffrey Stein, General Counsel, 1199 National Benefit Fund. We also thank representatives of the US Department of Labor with whom we have had informal conversations on several occasions. However, the opinions expressed in this paper are ours and we take full responsibility for them. We do not wish to imply that those who have contributed to our efforts either agree or disagree with the views we have expressed.

Moreover, legal advisors to plan fiduciaries who have a more refined understanding of the facts in a particular case may come to different conclusions about the appropriateness of trustee and plan expenses than the DOL has in the situations discussed in this paper.

Fiduciaries with the assistance of their professional advisors should use the information presented here as a resource along with other available information to evaluate their own practices, determine if they have any potential fiduciary exposure and implement changes if deemed necessary. We note that simple changes concerning documentation may make an enormous difference in the length, tone and ultimately the results of an investigation.

General Observations

This paper represents our understanding of the law and positions taken by the U.S. Department of Labor (DOL) concerning trustee and plan expense issues. The information has been collected from voluntary compliance letters in DOL investigations, DOL opinion letters, DOL Press Releases concerning suits and settlements, court decisions, statutes and regulations, the experiences of our professional colleagues and informal comments of DOL officials during conferences.

You should keep the following observations in mind as you review this paper:

- When the DOL comes to visit your plan it is conducting an investigation. It is seeking to detect and correct violations of the law. DOL representatives emphasized this point. In a case it considers appropriate, DOL will file a civil action to remedy violations. Some of the practices discussed in this paper may also be the basis for allegations of violation of criminal statutes applicable to persons dealing with employee benefit plans.

- Whether or not the DOL brings an enforcement action or demands correction concerning a particular issue will depend on the specific facts and circumstances of the alleged violation and the overall state of the plan's compliance with fiduciary and other requirements of the law. For example, if the practices of a plan and its fiduciaries and the documentation are substantially in accord with the principles discussed below, DOL might not question minor issues. However, if the overall practices of a plan show evidence of frequent and/or significant personal benefit to plan fiduciaries or employees, such as payment or reimbursement for expensive hotels, meals, and entertainment, the DOL is far more likely to challenge even small items that might otherwise be overlooked. Note that in its enforcement capacity, the DOL has the authority to pursue even the smallest violations. As a technical matter, there is no special rule under ERISA for fiduciary violations involving *de minimis* amounts, although as a practical matter, under certain circumstances, the DOL may choose not to pursue them.

- The fact that a particular practice may not have been challenged during an investigation of another plan in your area, does not establish that the practice is approved by DOL. By the same token, the fact that a practice was challenged either in an investigation in your area or in one of the cases to which we refer in this paper does not mean that this will be the DOL position in all cases. We have found significant differences in the DOL positions from case to case, region to region, and between the field offices and the DOL National Office.

- If there is a violation, DOL will require a fiduciary to reimburse the plan whether or not the plan's legal counsel or another plan professional has provided an opinion that the expense is reimbursable by the plan or reasonable in amount. Trustees are not protected by relying on such advice. The only way to avoid an assessment of liability by the DOL is to comply with its view of the rules concerning what expenses may lawfully be paid from plan assets. A process to establish reasonableness of expenses and documentation that the plan's process has been followed on a consistent basis will help to protect a fiduciary in that regard.

- Participants are likely to become aware of DOL allegations of self-dealing and inappropriate expenditures of plan assets. For example, the DOL usually issues a press release when it files a lawsuit or enters into a settlement. These press releases from 1994 to date are available on the DOL website.

- If suit is filed for breach of fiduciary duty, the plan itself may not be able to pay defense costs on behalf of fiduciaries. However, this is a complex topic and beyond the scope of this paper. If the plan cannot pay these defense costs and fiduciary insurance does not cover them, the trustee or plan employee will have to pay these costs personally. In addition, any amounts determined by the court to be owed back to the plan must either come from fiduciary insurance or the personal assets of the trustee or the plan employee who the court has found liable.

- In some circumstances, one plan fiduciary may be liable for the breaches committed by another plan fiduciary. For example, ERISA §405 provides that a fiduciary is liable for the actions of another fiduciary (1) if he knowingly participates in or undertakes to conceal a breach; (2) if by his failure to act prudently, he enables another fiduciary to commit a breach of duty; or (3) if he has knowledge of a breach of duty by another plan fiduciary and does not make reasonable efforts to remedy the breach of duty. In addition, some courts have found that fiduciary liability under ERISA is joint and several liability which means that each trustee found to have breached his or her fiduciary duty is liable for the entire loss to the plan. If some of the breaching fiduciaries are not financially able to pay their portion, the other fiduciaries will nevertheless be required to make the plan whole.

- It is probable, but not certain, that fiduciary insurance would cover at least some defense costs and would reimburse the plan for at least some losses, but fiduciary insurance should not be relied upon as a safety net for knowing violations. One should also keep in mind that the DOL could (and often does) seek to remove a trustee or plan employee involved in these matters. In addition, some of the transactions could also constitute criminal violations.

- The DOL generally will not settle claims for expense payments that it considers improper under the law (e.g., personal expenses) without full reimbursement back to the plan. The DOL will also require the trustee or plan employee who has received the benefit of improper expense payments by the plan to pay interest on any amounts paid back to the plan, as well as the 20% penalty required under Section 502(l) of ERISA. There is also a 15% excise tax on the amount of such transaction under the Internal Revenue Code. Depending on the policy, fiduciary insurance may not cover these additional penalties and assessments. The trustee or plan employee may also be required to reimburse the plan for any amounts impermissibly paid by a service provider to, or on behalf of, the trustee or plan employee even though the amounts were paid by the service provider and not directly with plan assets.

- Keep in mind that many expenses that are not reimbursable as a general rule may be reimbursable under the specific facts and circumstances involved. DOL makes this point repeatedly in opinions, Voluntary Compliance Letters and presentations. It is the fiduciary's responsibility to document the specific circumstances under which the fiduciary determines that an expense that might otherwise be viewed as personal or excessive is reimbursable.

- An expense must not only be of a type that is permissible under the law but the amount must also be reasonable under the circumstances involved. For example, a hotel room would be a permissible expense for a trustee traveling on plan business but if the amount of the hotel room far exceeded the amount for a comfortable and safe but not extravagant hotel reasonably convenient to the location of the meeting or conference, the excess would not be a reimbursable expense.

- The payment of plan assets for expenses to, or on behalf of, a trustee or plan employee that are not legitimate plan expenses, or are not reasonable is a prohibited transaction under ERISA.[2] Some of the practices discussed below may also be the basis for allegations of violation of criminal statutes applicable to persons dealing with employee benefit plans.[3] Fiduciary insurance usually does not cover criminal defense.

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[2] Section 406 (b) of ERISA provides that:

> [a] fiduciary with respect to a plan shall not –
> (1) deal with the assets of the plan in his own interest or for his own account,
> (2) in his individual or 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 interest of the plan or the interests of its participants or beneficiaries, or
> (3) receive any consideration for his own personal account from any party dealing with such plan in connection with a transaction involving the assets of the plan.

[3] 18 U.S.C 1954 provides:

Whoever being -

(1) an administrator, officer, trustee, custodian, counsel, agent, or employee of any employee welfare benefit plan or employee pension benefit plan; or
(2) an officer, counsel, agent, or employee of an employer or an employer any of whose employees are covered by such plan; or
(3) an officer, counsel, agent, or employee of an employee organization any of whose members are covered by such plan; or
(4) a person who, or an officer, counsel, agent, or employee of an organization which, provides benefit plan services to such plan

receives or agrees to receive or solicits any fee, kickback, commission, gift, loan, money, or thing of value because of or with intent to be influenced with respect to, any of the actions, decisions, or other duties relating to any question or matter concerning such plan or any person who directly or indirectly gives or offers, or promises to give or offer, any fee, kickback, commission, gift, loan, money, or thing of value prohibited by this section, shall be fined under this title or imprisoned not more than three years, or both: Provided, That this section shall not prohibit the payment to or acceptance by any person of bona fide salary, compensation, or other payments made for goods or facilities actually furnished or for services actually performed in the regular course of his duties as such person, administrator, officer,

- DOL has correctly pointed out that many plan expense violations can be corrected under the Department's Voluntary Fiduciary Correction Program. Information about this program is available on the DOL website at www.dol.gov/ebsa. Although a plan must follow the procedure to gain the full range of protection offered by the program, we have heard DOL representatives comment at conferences that they understand that some plans may choose to do the correction without filing. Our own experience has been that self-correction of a violation will be looked upon favorably by DOL. In any event, self-correction will significantly limit the amount that may be owed by a fiduciary.

We emphasize again that to understand the background, intent, and import of the Questions and Answers below requires a careful reading of the Introduction. As previously noted, these answers represent a compilation of existing DOL guidance and other information regarding DOL enforcement policy or positions gained through personal experiences by us and others who been involved in DOL investigations; these answers are not legal guidance or definitive guidelines. The facts and circumstances, including the documentation process of each case, are critical to whether DOL chooses to find and pursue a violation. Significant differences exist in the way in which DOL has treated certain issues, in large part due to the underlying circumstances of a particular case, but also because of differences among individual investigators, different regional offices of DOL and between the field offices and DOL National Office. Fiduciaries should consult their legal advisors to determine how these DOL policies may apply in any given case.

General Plan Expense Rules

1. For what purposes may plans assets be expended?

Plan assets may only be expended to pay benefits to participants and beneficiaries and to defray the reasonable expenses of administering the plan. ERISA § 404(a)(1)(A). In making determinations concerning plan expenses a fiduciary must discharge his duties "solely in the interest of participants and beneficiaries." ERISA §404(a)(1)(A). This is the first question that a DOL investigator usually addresses so you need to be prepared to show how each questioned expense benefits participants and beneficiaries. If an expense is permissible under this test, the amount must also be reasonable as discussed below.

As will be discussed below, plan assets may not be expended to benefit a party in interest. This would prohibit a variety of expenditures including (1) the personal expenses of a fiduciary or plan employee, or (2) expenditures pursuant to a services sharing arrangement in which a plan pays more than its share of expenses based on time allocations. Also prohibited are expenditures for gifts or items of value of a personal nature to trustees, plan employees, and service providers. However, the

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trustee, custodian, counsel, agent, or employee of such plan, employer, employee organization, or organization providing benefit plan services to such plan.

As used in this section, the term (a) "any employee welfare benefit plan" or "employee pension benefit plan" means any employee welfare benefit plan or employee pension benefit plan, respectively, subject to any provision of Title I ofERISA, and (b) "employee organization" and "administrator" as defined respectively in section 3(4) and (3)(16) of ERISA.

plan may compensate a trustee, service provider or plan employees within the restrictions of ERISA § 408. *See* Q&A 3 and 6. Remember that a party-in-interest to a plan includes trustees, plan employees, service providers, the union, participating employers and employer associations as well as a related plan if one or more trustees of a plan also serve as trustees of the other plan.

This paper addresses the purposes for which plan assets may be expended and the rules applicable to plan assets. Keep in mind that plan assets may not be expended in connection with a function performed in a settlor capacity. A discussion of this topic is beyond the scope of the paper but we have been advised that the DOL has questioned expenses in connection with plan actions that could be considered settlor functions under existing case law. *See* DOL Field Assistance Bulletin 2002-2.

We have been advised that DOL added a question to a number of 2005 investigations asking whether the plan had expended plan assets to "influence public policy" in connection with the Social Security debate. In May 2005, Alan Lebowitz, Deputy Assistant Secretary for Programs Operations sent a letter to the AFL-CIO setting forth DOL's views that ERISA violations would occur if plan fiduciaries expend plan assets to inform participants about the public debate on Social Security or hire or fire plan service providers based upon the service providers' opinions on Social Security reform.

2. What is the general rule for the payment or reimbursement of expenses?

As noted above, a fiduciary must discharge his duties "solely in the interest of participants and beneficiaries" and must act prudently when making determinations concerning plan administrative expenses. ERISA §404(a)(1)(A) and (B).

This paper focuses primarily on the payment or reimbursement of the expenses of plan fiduciaries such as travel-related expenses. However, it also addresses issues concerning a plan's compensation of fiduciaries, plan staff and service providers.

Payment to a Party in Interest for Services to the Plan: Section 408(b)(2) of ERISA provides an exemption from the prohibitions of ERISA §406(a) if a plan contracts or makes reasonable arrangements with a party in interest, including a plan fiduciary, for office space or services necessary for the establishment or operation of the plan if no more than reasonable compensation is paid for the space or services.

Fiduciary Compensation and Expenses: In addition to the rule above permitting reasonable arrangements for space and services, another section of ERISA addresses compensation and expenses to plan fiduciaries. This rule provides that a plan fiduciary may receive reasonable compensation from a plan for services rendered to the plan as well as reimbursement for reasonable "direct expenses" properly and actually incurred in the performance of his duties with the plan and not otherwise reimbursed. ERISA §408(c)(2); DOL Reg. §2550.408(c)-2(b)(2). However, a fiduciary who is already receiving full-time pay from an employer, employer association or a union whose members participate in the plan, may only receive reimbursement for reasonable "direct expenses" properly and actually incurred in the performance of his duties with the plan and not otherwise reimbursed. ERISA §408(c)(2); DOL Reg. §2550.408(c)-2(b)(2). An expense is not a "direct expense" to the extent it would have been sustained even if the service had not been provided. DOL Reg. §2550.408(c)-2(b)(3). An expense may not be reimbursed unless it is properly documented.

Therefore, the issue of fiduciary compensation is closely related to the issue of reimbursement for expenses and is discussed in Q&A 3.

Compensation and Fee Issues

3. May a fiduciary receive compensation from a plan?

Section 408(b)(2) of ERISA provides an exemption from the prohibitions of ERISA §406(a) if a plan contracts or makes reasonable arrangements with a party in interest, including a plan fiduciary, for office space or services necessary for the establishment or operation of the plan if no more than reasonable compensation is paid for the space or services. Such services could include services as a plan administrator or trustee. The plan fiduciaries making the contract or arrangement must determine that the office space or service is --

- necessary for the establishment or operation of the plan, and
- furnished under a contract or arrangement that is reasonable.

In addition, fiduciaries must determine that no more than reasonable compensation is paid for the office space or service. Having contemporaneous documentation of these determinations and the basis on which they were made may be helpful in a subsequent DOL investigation.

These standards apply to compensation arrangements for a fiduciary including a plan trustee, plan staff (Q&A 5), service providers (Q&A 9), as well as compensation to the union, an employer or association or a related plan for services (Q&A 8).

However, §408(b)(2) does not provide an exemption for acts of fiduciary self-dealing as described in ERISA §406(b)(1) (relating to fiduciaries of the plan dealing with the assets of the plan in their own interests or for their own account, i.e., personal benefit); §406(b)(2) (relating to fiduciaries of a plan in their individual or any other capacity acting in any transaction involving the plan on behalf of a party whose interests are adverse to the interests of the plan or its participants and beneficiaries); or §406(b)(3) (relating to fiduciaries receiving consideration for their own personal account from any party dealing with the plan in connection with a transaction involving plan assets).

Therefore, §408 exempts the payment of reasonable compensation, including expenses, by a plan to plan fiduciaries and other parties in interest for services provided but not acts of self-dealing, including compensation or expenses, that would be prohibited by ERISA §§ 406(b)(1), (2) or (3).

We emphasize that the expense must be for a necessary service or office space. DOL Reg. § 2550.408b-2(b) states that a service is necessary if the service is appropriate or helpful to the plan in carrying out the purposes for which the plan is established. In other words, fiduciaries should ask themselves how the expense benefits participants and beneficiaries of the plan and the basis for this determination should be documented.

As discussed above, a plan fiduciary (including a plan trustee) may receive reasonable compensation from a plan for services rendered to the plan as well as reimbursement for reasonable direct expenses properly and actually incurred in the performance if his duties with the plan and not otherwise reimbursed. ERISA §408(c)(2); DOL Reg. §2550.408(c)-2(b)(2). However, a fiduciary who is already receiving full-time pay from an employer, employer association or from a union whose members participate in the plan, may only receive reimbursement for reasonable direct expenses properly and actually incurred in the performance of his duties with the plan that are not otherwise reimbursed. ERISA §408(c)(2); DOL Reg. §2550.408(c)-2(b)(2).

A plan fiduciary who is not already receiving full-time pay from a union, employer or employer association may be paid reasonable compensation for services to the plan. For such a fiduciary, the plan may pay the compensation and reimburse expenses. The compensation could be used by the fiduciary for any purpose including paying expenses that the plan could not reimburse.

Whether or not a fiduciary is receiving full-time pay from a union, employer or employer association is not always easy to determine. There are no regulations defining "full-time pay" for this purpose and DOL has stated that this must be determined on the basis of all the facts and circumstances. However, DOL issued a General Information Letter on June 4, 1993 that states the Department's view that "an employee who is compensated on an hourly basis and who suffers a loss of pay by reason of his absence from work while performing duties as a fiduciary does not receive full-time pay within the meaning of section 408(b)(2)." However, the Information Letter also expressed the view that "in most cases, an individual who is paid a salary for services for an employer [or the union] would be receiving full-time pay." In *Gilliam v. Edwards,* 2 EBC 2475, 2483 (D. N.J. 1980) the court addressed the full-time pay requirement: "Edwards' business-agent salary entitlement from the union—an employee organization whose members are plan participants—was substantial enough to qualify as full-time pay for purposes of the fiduciary rationale of the rule. ERISA focuses, not on the hours devoted to the second job or function, but on the amount of payment received. Its aim is to prevent double payment from a party in interests, S. REP. No. 383, 93d Cong., 2d Sess. 3, *reprinted in* U.S. CODE CONG. & AD. NEWS 4890, 4983, and thus avoid the conflicts dual allegiances may spark. A weekly salary of even $250 [in 1980] is sufficient to create an impermissible interest tension."

In Advisory Opinion 76-03, DOL determined that, in the case of the owner of a business who was absent from his business to perform his duties for a plan, "it is unlikely the trustee's regular full-time pay or compensation will be diminished by his time spent on plan duties."

In a July, 1988 Information Letter in response to a request submitted by our office, a trustee was required to reimburse an expense advance stolen from him before he left for the conference. Since the trustee was already compensated for full-time services by the union, he could only be reimbursed for expenses actually incurred. The stolen expense advance did not represent expenses actually incurred.

It is most important to keep in mind that a fiduciary should not be involved in determining his own compensation. Thus, a trustee who is able to be compensated because he is not receiving full-time pay should not take part in the decision whether to pay compensation to trustees or the amount of the compensation. Similarly, a plan administrator should not establish his own compensation or take part in the compensation decision. This would violate ERISA §406(b) even though the payment of the compensation itself would be permitted. This is explained very well in DOL Regs. §2550.408b-2(e):

> The prohibitions of section 408(b) supplement the other prohibitions of section 406(a) of the Act [ERISA] by imposing on parties in interest who are fiduciaries a

> duty of undivided loyalty to the plans for which they act. These prohibitions are imposed upon fiduciaries to deter them from exercising the authority, control, or responsibility which makes such persons fiduciaries when they have interests which may conflict with the interests of the plans for which they act. In such cases, the fiduciaries have interests in the transactions which may affect the exercise of their best judgment as fiduciaries. Thus, a fiduciary may not use the authority, control, or responsibility which makes such person a fiduciary to cause a plan to pay an additional fee to such fiduciary (or a person in which such fiduciary has an interest which may affect the exercise of such fiduciary's best judgment as a fiduciary) to provide a service. Nor may a fiduciary use such authority, control, or responsibility to cause a plan to enter into a transaction involving plan assets whereby such fiduciary (or a person in which such fiduciary has an interest which may affect the exercise of such fiduciary's best judgment as a fiduciary) will receive consideration from a third party in connection with such transaction. A person in which a fiduciary has an interest which may affect the exercise of the fiduciary's best judgment as a fiduciary includes, for example, a person who is a party in interest by reason of a relationship to such fiduciary described in section 3(14)(E), (F), (G), (H), or (I).

Persons described in section 3(14)(E), (F), (G), (H), or (I) include persons having interests in an employer or union; or an entity with specified ownership interests by a plan fiduciary, a plan service provider, a participating employer, participating union or relative of a fiduciary, service provider, employer or union official.

The regulation also includes several good examples. Example 7 illustrates how fiduciaries may avoid engaging in a prohibited transaction in connection with decisions involving their own compensation arrangements. In this example, one trustee of a plan is president of a bank and the bank proposes to provide services to the plan. The example states that this trustee physically absents himself from all consideration of the proposal and does not otherwise exercise any of the authority, control or responsibility which makes him a fiduciary to cause the plan to retain the bank's services. The other trustees of the plan consider the matter and decide to retain the bank. The example, concludes that the bank president/trustee has not violated §406(b)(1) of ERISA. It also states that the other trustees have not violated §406(b)(1) merely because the president of the bank is a trustee of the plan. This fact alone does not cause the other trustees to have an interest in the transaction which might affect the exercise of their best judgment as fiduciaries.

Gilliam v. Edwards, 2 EBC 2475 (D. N.J. 1980) explains that "a combined reading of §§1106 and 1108 [ERISA §§406 and 408] and the relevant regulation suggests that a fiduciary normally permitted to receive reasonable compensation for services rendered—the purpose of the §1108 exemption is to preserve this rule—may not if self-dealing is involved in the transaction securing the payment." *Id. at 2482*. In this case, the court found a violation where a plan trustee actively participated in the trustee decision to hire himself as plan administrator. The court found that this clearly indicated that trustee's abandonment of his fiduciary obligation to secure for the Fund the best contract possible. The court noted :

> In a §1106(b) context, the Third Circuit has required plans to be represented 'by trustees who are free to exert the maximum economic power manifested by their

> fund whenever they are negotiating a commercial transaction.' *Cutaiar v. Marshall,* 590 F. 2d at 350. A leading trust authority observed:
>
> Reasons behind the establishment of the loyalty rule by equity are that it is generally, if not always, humanly impossible for the same person to act fairly in two capacities and on behalf of two interests in the same transaction. Consciously or unconsciously he will favor one side as against the other, where there is or may be a conflict of interest. If one of the interests involved is the trustee personally, selfishness is apt to lead him to give himself an advantage. If permitted to represent antagonistic interests the trustee is placed under temptation and is apt in many cases to yield to the natural prompting to give himself the benefit of all doubts. G. BOGERT, TRUSTS AND TRUSTEES §543, at 475-76 (2d ed. 1960).

Although not directly related to the issue of when a fiduciary may receive compensation from a plan, it is worthy of note that the IRS has determined, in a March 2004 ruling in response to a determination of employment status for Federal employment tax purposes, that paid trustees were "employees" of the multiemployer welfare fund that paid them. The IRS noted that the individual trustees' assignments were determined by the Board as a whole. After reviewing the facts concerning the relationship of these trustees to the Board as a whole, the IRS concluded that the workers (trustees) "are employees of the firm for Federal employment tax purposes, and not independent contractors engaged in their own trade or business."

4. What is a reasonable expense of plan administration?

Plan assets may not be used to pay expenses unless the amount is reasonable and the expenditure is for the administration of the plan. ERISA §404(a)(1)(A)(ii). The reasonableness standard applies to <u>all</u> plan administrative expenditures. When the plan determines the compensation package for a plan fiduciary or plan staff, hires a service provider, or buys equipment or a building or leases space, this standard applies.

Reasonableness is determined by the circumstances and is based on what a fiduciary would prudently expend in like circumstances for the sole and exclusive interest of participants and beneficiaries. ERISA §§404(a)(1)(A)(ii) and 404(a)(1)(B). Since ERISA §404(a)(1)(B) requires that prudence be determined in the "conduct of an enterprise of like character and with like aims," the standards applicable to ordinary business expenditures generally do not apply since the assets of the plan are held by fiduciaries in trust for the participants and beneficiaries and are not used in the conduct of a business for profit.

Therefore, before plan assets may be used to pay an expense, the expense must be <u>both</u> for the administration of the plan and reasonable in amount. An expense may be reasonable in amount but not for the administration of the plan, such as union or employer expenses or personal or recreational expenses of a trustee or plan employee, in which case plan assets cannot be used for the expense. Or an expense may be a proper administrative expense of the plan but not reasonable in amount, in which case plan assets may not be used for the portion of the expense that is excessive.

DOL investigations often involve issues concerning the fees paid to service providers. *See* Q&A 9 for a brief discussion of service provider compensation issues.

Plan administrative expenses must be approved by plan trustees and not by the plan administrator. This involves the exercise of "trustee responsibilities," which means the responsibility provided in the plan's trust to manage or control the assets of the plan. ERISA § 405(c) provides that "trustee responsibilities" may only be delegated to a trustee or, in the case of investment responsibilities, an investment manager. In Advisory Opinion 81-21A, the DOL concluded that the trustees of a joint apprenticeship fund may not transfer plan assets for the joint apprentice committee to use to fund the operations of the plan since the committee did not include any trustees.

We believe that the trustee may exercise this control by establishing a policy, formula or budget that is implemented by the plan office. Policies involving trustee compensation and the issues discussed in this paper should be adopted by the trustees who must determine and document the benefit to the plan. The issue involving trustee approval of actions involving plan assets was raised by the DOL in an investigation in which we were involved. DOL challenged the allocation of collected contributions among related plans by the administrator. However, the DOL yielded when presented with the written allocation policy adopted by the trustees and implemented by the administrator.

5. What are the rules concerning compensation to plan staff?

As stated above, the reasonableness standard applies to compensation issues for plan staff. DOL investigations generally focus on a limited number of staff compensation issues such as gifts, holiday parties and amenities for plan staff. Some of these issues are addressed in separate Q&A's below.

One issue that does come up involves severance pay or retirement bonuses which the DOL has challenged unless agreed to prior to the termination as an inducement to keep the individual employed. In Advisory Opinion 81-83A, the DOL found that a payment made to the plan's executive director as part of his severance package was unreasonable since it did not constitute compensation under ERISA §408. Similarly, in Advisory Opinion 89-08A, the DOL found that a special benefit paid to a training director upon his retirement was unreasonable. The apprentice director had received a salary for his years of service to plan. When he announced his retirement, the trustees decided to give him additional compensation in the form of a retirement benefit. In finding that the retirement benefit was unreasonable, the DOL found that the benefit constituted inappropriate compensation for services rendered in the past and was in addition to the salary package originally agreed upon in the employment relationship. Because the additional benefit was not part of the director's expectation of compensation for his services rendered to the plan, it was unreasonable compensation under ERISA §408.

It is important to remember that the compensation package for a plan employee includes more than just the salary paid. For some positions, particularly where the plan seeks to attract and retain a highly qualified individual, the compensation package may include other benefits such as a car, non-qualified retirement arrangements, bonuses, severance arrangements, travel arrangements. So long as the package is documented and reasonable, the individual components of the package should be permissible. *See* Q &A 20 for additional information.

6. May a plan give gifts to plan staff? May a plan give gifts or donations of any kind to anyone else?

We have been advised of several investigations in which the DOL has disallowed gifts: flowers sent to a trustee or a trustee's spouse upon the illness or death of the trustee or spouse; flowers to a plan employee upon the death of a family member; flowers to a terminally ill plan employee; flowers to a retiring service provider; flowers to a seriously ill service provider.

In a recent Voluntary Compliance Letter, the DOL stated its position that such expenditures were non-exempt prohibited transactions for which clear guidance is provided in ERISA §3(14)(A) & (B) and §404 and §406(a)(1)(C) &(D). DOL reiterated that a fiduciary must discharge his duties solely in the interest of participants and beneficiaries and for the exclusive purpose of providing benefits and defraying reasonable administrative expenses. In the DOL's view in that investigation, these kinds of expenses did not satisfy those requirements. In another case, the DOL agreed not to require reimbursement from the trustees for flowers sent to a plan employee in sympathy for her dying mother and flowers to a terminally ill employee if the plan agreed not to send flowers in the future in similar cases.

At least in the case of such kindnesses to plan employees, we understand that this hard line against payment of these types of expenses from plan assets is not necessarily the position of the National Office. Also various regional offices may take different positions. Sending flowers on occasions such as those described above to plan staff are important for staff morale which affects productivity and employee retention. Trustees could reasonably determine and document the determination that such actions benefit participants. A different standard, however, might apply to gifts to plan staff than would apply to gifts to plan service providers or others. Moreover, if such items were included in a collective bargaining agreement covering plan staff, they would be part of the bargained-for compensation package (for example, a holiday bonus or food certificate).

In *Dole v. Formica*, 14 EBC 1397 (N.D. Ohio 1991), the court found that the trustees violated their fiduciary duties by making various gifts and donations. "It is no defense that the trustees believed that these gifts and donations benefited the plans by creating good will, showing appreciation or encouraging employers to make the required contributions. These expenses are not made in the sole interest of the participants for the exclusive purpose of providing benefits and defraying costs." *Id. at 1410*. There is no information about the nature of the gifts and donations involved.

Based on the input we have received from various sources, it appears that DOL might permit flowers or similar expressions of sympathy or joy for plan employees based upon a documented trustee determination of benefit to the plan and its participants. However, we have not found affirmative evidence that DOL has approved flowers, plaques or other items for births, death, retirements for non-employees including trustees and service providers or donations to charities or other events.

One of the interesting aspects of the position taken by some DOL investigators regarding expenditures for *de minimis* gifts (such as flowers) is the potential difference in treatment between self-administered plans and those using a third-party administrator (TPA). We have not heard of instances in which the DOL has questioned TPAs about similar expenditures. These *de minimis* gifts and kindnesses are clearly considered part of the compensation arrangement offered by TPA firms and these firms often compete with self-administered plans for employees. The same concerns regarding differential treatment between plan employees and TPA employees apply to Q&A 8 below.

Finally, we suggest that a plan's auditor be consulted concerning the taxability of gifts to employees.

7. May a plan provide a holiday party, picnic, luncheons or refreshments for plan employees or participants?

This issue has caused a great deal of controversy and we have been advised that DOL has raised it in several investigations across the country. While a plan may provide its employees with reasonable compensation and benefits, some plans have been challenged when the plan pays for a holiday party for its staff. In some cases, DOL has also challenged plans' payment for other extras that are often provided to employees for morale, such as coffee, bagels or donuts, staff luncheons or retirement parties.

In response to an inquiry, a DOL investigator rejected a proposal by the plan trustees to adopt a policy allocating an amount per employee per year as part of the employees' compensation package to cover incidental employee expenses including Christmas parties, retirements, birthdays, donuts, bagels, flowers and similar items. The Trustees had concluded that such minimal amenities were necessary to maintain the morale and productivity of plan employees and that maintaining a satisfied and productive workforce directly benefited participants and beneficiaries. In response, the DOL investigator reiterated its position that providing Christmas parties, birthday cakes, retirement parties, donuts, bagels, flowers and similar items to a party in interest (plan employees) violates ERISA §§404(a)(1)(A),(B) and (D) and 406(a)(1)(D). The DOL investigator asserted that there are no statutory or class exemptions allowing prohibited transactions. We understand that, subsequently, the DOL advised that the plan could provide a more modest holiday party for its staff based upon a trustee determination of the benefit to the plan and its participants; however, the DOL would not approve the original budget proposal.

In another investigation, the DOL investigator originally disallowed the entire cost of a holiday party. Counsel to the plan argued with the investigator based on the positions described below and ultimately the DOL only required reimbursement for service providers who attended the party, not for plan employees. In yet another investigation, the DOL initially challenged a holiday party and occasional pizza for plan staff but finally allowed these expenses.

It is unclear to us whether the position taken by some DOL investigators with respect to these issues reflects the view of the DOL National Office.

However, we believe that such expenses can be justified as part of plan employees' compensation package. In addition, such expenses benefit participants and beneficiaries since they improve employee morale, productivity and particularly employee retention. Section 408(b)(2) of ERISA provides a statutory exemption from the prohibitions of section 406(a) for contracting or making reasonable arrangements with a party-in-interest for services necessary for the establishment or operation of the plan, if no more than reasonable compensation is paid for such services. Employee compensation is clearly covered by this exemption or a plan would be unable to pay salaries or provide benefits to its own employees. The additional compensation in the form of minimal amenities is no different than salaries; it is part of the total compensation package. In addition, many plans with their own staff compete with third party administrators for employees. The plan's compensation package must be competitive with the total compensation package offered by third party administrators and those packages generally include such minimal amenities.

Given the position of some DOL investigators, a plan should be very cautious concerning such expenses for plan employees. To provide some protection, the trustees of a plan (not the administrator) must make the determination that such expenses benefit participants and beneficiaries and the basis for the decision must be documented. In addition, the amount of the expense incurred should be modest or it will invite DOL challenge. A plan should not pay for retirement parties for trustees. Because the plan may not pay for such expenses, we do not believe that a service provider could pay for them either.

We were advised of a 2005 investigation in which the DOL challenged a Holiday buffet that a plan provided to retirees and their spouses. The Plan argued that it was a plan benefit to participants and beneficiaries. The DOL then noted that this benefit was not provided for in the Plan document and, therefore, its payment was not in accordance with Plan documents.

8. How should shared expenses be allocated among related plans and related organizations?

Transactions between plans with common trustees are generally prohibited transactions. However, soon after ERISA was enacted, the DOL issued class exemptions permitting related plans to share administrative services and office space. *See* Prohibited Transaction Class Exemptions 76-1 and 77-10. The exemptions also permit a plan to share administrative services and office space with an organization that is a party-in-interest (such as a union, an employer or an employer association).

When related plans share services or office space, each plan should pay its own direct expenses. Shared expenses should be allocated among the plans based on objective time studies. Our experience in several investigations has been that DOL permits collection-related expenses to be allocated based on the contribution rate of each plan or other entity. However, our experience is that DOL also requires that data input functions concerning remittance reports be allocated equally to all plans and organizations reported on the form. The trustees of the plan and not the administrator should update and approve the allocation at least annually.[4]

This issue is often a focus of the DOL in its investigations. DOL is looking for allocations that are skewed to benefit smaller plan or organizations. For example, the union or industry promotion fund or the welfare or individual account pension plan may be given a lower allocation than would be required based on time studies. Resist the temptation to do this. In our experience in several investigations, the plans and organizations that benefited from the lower allocation must repay the other plans. The DOL has required the payments to go back as much as six years.

Any arrangement with a plan for sharing administrative services or office space with a party-in-interest, such as the union, a contributing employer or a related plan, must comply with the requirements of Prohibited Transaction Class Exemptions 76-1 and 77-10.[5] Sharing services with a

[4] One of our clients requires plan employees to fill out time sheets and expenses were allocated based on actual time. A subsequent DOL investigation ended very quickly when DOL was advised that all shared expenses were allocated based on actual time records.

[5] Prohibited Transaction Class Exemptions 76-1 and 77-10 apply when a multiemployer obtains office space or services and share the space or services with a party-in-interest. PTE 76-1 provides an exemption from ERISA §406(a). PTE 77-10 provides an exemption from §406(b) so that trustees of related multiemployer plans that share services with each other can approve the arrangement. These Prohibited Transaction Exemptions do not apply when a plan makes arrangements to obtain space or services FROM a party-in-interest such as a union or employer. There is an exemption for such arrangements in 406(b) so that trustees of related multiemployer plans that share services with each other can

plan or organization that is not a party-in-interest is not covered by these Exemptions but the fiduciary requirements concerning reasonableness of fees paid or received by the plan for services would apply. In addition, PTE 76-1 requires that the "costs of securing such space, services and goods are assessed and paid on a pro rata basis with respect to each party's use of such space, services and goods." This requires an allocation of actual costs and not, for example, the assessment of rent based on the rental market in the area. However, a comparison to the rental market is important to establish the reasonableness of the rent. A plan renting from a union or employer would be permitted to pay its proportionate share of the actual costs but no more than the plan would pay if it rented from a third party in the area.

9. What are the plan fiduciaries' responsibilities concerning service provider compensation and fees?

Plan fiduciaries' responsibilities include the prudent selection and monitoring of service providers. The selection and monitoring activities include determining reasonable compensation for service providers both when the service provider is initially retained and on an ongoing basis. The DOL has issued piecemeal guidance on selection and monitoring of service providers:

In DOL Regulations §2509.75-8 - Questions and answers relating to Employee Retirement Income Security Act, Q&A FR-17 the DOL addressed the ongoing responsibilities of a fiduciary with respect to appointments:

> A: At reasonable intervals the performance of trustees and other fiduciaries should be reviewed by the appointing fiduciary in such manner as may be reasonably expected to ensure that their performance has been in compliance with the terms of the plan and statutory standards, and satisfies the needs of the plan. No single procedure will be appropriate in all cases; the procedure adopted may vary in accordance with the nature of the plan and other facts and circumstances relevant to the choice of the procedure.

In a 1997 Information Letter, the DOL advised:

> In selecting a service provider such as an enrolled actuary, the responsible plan fiduciary must engage in an objective process designed to elicit information necessary to assess the qualifications of the service provider, the quality of the work product, and the reasonableness of the fees charged in light of the services provided. In addition, such process should be designed to avoid self-dealing, conflicts of interest or other improper influence. What constitutes an appropriate method of selecting a service provider, however, will depend upon the particular facts and circumstances. Soliciting bids among service providers at the outset is a means by which the fiduciary can obtain the necessary information relevant to the decision-making process. Whether such a process is appropriate in subsequent years may depend, among other things, upon the fiduciary's knowledge of the service provider's work

approve the arrangement. These Prohibited Transaction Exemptions do not apply when a plan makes arrangements to obtain space or services FROM a partyin-interest such as a union or employer. There is an exemption from §406(a) for such arrangements in ERISA §408(b)(2) but there is no exemption from §406(b) so conflicted trustees must recuse themselves from decisions concerning any such transaction.

> product, the cost and quality of services previously provided by the service provider, the fiduciary's knowledge of prevailing rates for the services, as well as the cost to the plan of conducting a particular selection process. Regardless of the method used, however, the fiduciary must be able to demonstrate compliance with ERISA's fiduciary standards.
>
> Because a number of factors will necessarily be considered by a fiduciary when selecting a service provider, a fiduciary need not necessarily select the lowest bidder when soliciting bids, although the compensation paid to the service provider by the plan must be reasonable in light of the services provided. The fiduciary should not consider one factor, such as the lowest fee bid for services, to the exclusion of any other factor, such as the quality of the work product. Rather, the decision regarding which service provider to select should be based on an assessment of all the relevant factors, including both the quality and cost of the services.

DOL placed even more emphasis on the quality issue in a 1998 Information Letter. After a statement very similar to that quoted above, the Department stated:

> It should be noted that, because "quality of services" is a factor relevant to selection of a service provider, it is the view of the Department that a plan fiduciary's failure to take quality of services into account in the selection process would constitute a breach of the fiduciary's duty under ERISA when, in the case of a Taft-Hartley or other plan, the selection involves the disposition of plan assets.

In 2002, the DOL issued Advisory Opinion 2002-08A concerning the attempts of service providers to limit liability and the process for selection of service providers. It again stated the standards for selection of service providers in language almost identical to the 1997 Information Letter. With respect to the limitation of liability provisions, it stated:

> Soliciting bids among service providers is a means by which a fiduciary can obtain the necessary information relevant to the decision-making process, including information about contractual provisions such as those identified in your letter relating to limitations of liability and indemnification.
>
> The Department does not believe that, in and of themselves, most limitation of liability and indemnification provisions in a service provider contract are either per se imprudent under ERISA section 404(a)(1)(B) or per se unreasonable under ERISA section 408(b)(2). The Department believes, however, that provisions that purport to apply to fraud or willful misconduct by the service provider are void as against public policy and that it would not be prudent or reasonable to agree to such provisions. Other limitations of liability and indemnification provisions, applying to negligence and unintentional malpractice, may be consistent with sections 404(a)(1) and 408(b)(2) of ERISA when considered in connection with the reasonableness of the arrangement as a whole and the potential risks to participants and beneficiaries. At a minimum, compliance with these standards would require that a fiduciary assess the plan's ability to obtain comparable services at comparable costs either from

service providers without having to agree to such provisions, or from service providers who have provisions that provide greater protection to the plan.

See DOL Information Letter dated February 23, 2005 concerning the conduct of a trustee involved in a selection process for a service provider at www.dol.gov/ebsa/regs/ILs/il022305.html.

In a recent Voluntary Compliance Letter, the DOL commented that a plan fiduciary's approval of a service provider's annual retainer "without any accounting for services rendered may constitute violations of ERISA Sections 404(a)(1)(A),(B) & (D)." The Department stated that it was concerned with the 'objective process' undertaken by the Trustees and recommended that in the future the process and analysis be set forth in plan documents.

The obligation to review compensation arrangements on an ongoing basis is not limited to retainer arrangements and is not limited to just the fee rate. It applies to all aspects of the service provider compensation package including expense reimbursements and limitations of liability provisions. However, there is little guidance beyond general principles concerning the method of monitoring the performance of service providers particularly those service providers such as the actuary, accountant, lawyer, etc. where performance cannot be measured against a numerical benchmark.

Other recent developments indicate a continued focus on fees by DOL, private plaintiffs, and various regulatory arms of the States. DOL has recently proposed revisions to Form 5500 including a revised Schedule C "Service Provider Information" which requires detailed disclosure of fees paid directly or indirectly to plan service providers. The new requirement would generally be effective for the 2008 plan year. In October 2006, suits were filed against seven major corporations alleging ERISA fiduciary violations in connection with allegedly high fees paid by 401(k) plans. In addition, New York Attorney General Eliot Spitzer is reportedly close to reaching a settlement with a major insurance company that sells and oversees 401(k) programs for taking undisclosed fees to promote certain mutual funds for a retirement fund for teachers.

Travel and Related Expense Issues

10. May a plan reimburse any personal expenses incurred while the trustee or employee is traveling?

A plan may not reimburse any personal expenses. Personal expenses include all items that would be paid for by the trustee or employee personally while at home. Personal items do not involve the administration of the plan. We have been advised by our colleagues or have found cases, Voluntary Compliance Letters or Press Releases showing that the DOL has challenged plan reimbursements to fiduciaries for movies, health club fees, massages, spa fees, medications, magazines, newspapers, gift shop purchases, entertainment, cigars, alcohol, bottled water, toiletries or similar items or services and, of course, any expenses for spouses, family or guests. According to the DOL, the difference, if any, between a hotel's single occupancy rate and a double occupancy rate is a personal expense. Dry cleaning and laundry services are also generally personal expenses.

Keep in mind as you read the following sections what we initially pointed out in the Introduction about the necessity to consider the applicability of the DOL enforcement positions described below in light of the facts and circumstances of each case. This section lists various expenses challenged by the DOL in individual investigations around the country.

Except for the matters in which we were involved, we do not know the factual context of these cases. With respect to reported cases and press releases, we are only aware of the facts as reported. Also keep in mind that documentation of the plan fiduciaries' determination why an expense is plan-related could be determinative.

We understand the DOL's position to be that a plan may not reimburse personal expenses that a fiduciary incurs because he or she is traveling on plan business. This would mean, for example, that long distance phone calls or internet services not related to plan business may not be reimbursed simply because the individual is away from his/her regular place of business. To the extent that charges for phone calls and internet fees related to plan business can be determined, they may be reimbursed. Documenting these expenses is critical.

In *McLaughlin v. Tomasso*, 9 EBC 2438 (E.D.N.Y. 1988), a case brought by DOL, the court found that the trustees of a plan breached their fiduciary duties by spending too large a percentage of the plan's income on administrative expenses. The DOL specifically pointed out telephone charges among the unlawful expenses. *Id*. at 2448. In a 1991 Voluntary Compliance Letter, the DOL listed charges for excessive phone calls as amounts to be reimbursed by trustees stating that the calls appeared to have no purpose related to plan business. In a July, 1996 press release, the DOL announced that it was suing some New York benefit plans partly for leasing expensive cars equipped with cellular telephones which were used by numerous plan employees *without determining the reasonableness or necessity of such use*. In a March, 1997 press release, the DOL stated that it sought reimbursement of expenses and a permanent injunction against the trustees of a welfare plan for using plan assets to pay for personal expenses of fiduciaries including cellular phones.

See also Q&A's 11, 12, 13, 14, 16, 21, 25, which address related issues.

11. May a plan reimburse any business expenses that are not plan-related but are incurred while the trustee or employee is traveling?

We understand the DOL's position to be that a plan should not reimburse any business expenses that are not plan-related, such as phone calls or faxes for union or employer business. Such expenses do not involve the administration of the plan because they are not incurred in the performance of the person's duties <u>for</u> the plan; rather, they are incurred because the individual continues to conduct other business while traveling. Such expenses have been challenged in several cases but, in others, the DOL did not address the question of phone calls.

In contrast to the reasoning of DOL in the cases described above, counsel have argued that such phone calls by fiduciaries concerning personal or non-plan related business matters are reasonable expenses of plan administration. Just like the expense for the hotel room that would not be incurred if the fiduciary were not traveling on plan business, the long distance phone calls would not be incurred if the fiduciary were not traveling on plan business. DOL Regs. §2550.408c-2(b)(2) provides for the reimbursement of *direct* expenses properly and actually incurred. §2550.408c-3 states that "an expense is not a direct expense to the extent it would have been sustained had the service not been provided," It seems that expenses for long distance phone calls incurred because a fiduciary is traveling on plan business meet this definition. However, the amount of the expense for such calls must also be reasonable.

In any event, we believe that a modest amount for phone calls is unlikely to be challenged by DOL. If phone expenses are high, a fiduciary should be prepared to document the plan business for which the phone calls were made. We have been advised from several sources that the DOL has examined phone calls on hotel bills and required the fiduciary to annotate each phone call to document that it was plan business. In view of the high phone expenses that may be incurred using a hotel phone, our suggestion is to use cell phones or telephone calling cards whenever possible.

In a Voluntary Compliance letter issued in 1991, the DOL challenged phone calls made by the trustees to conduct their business while traveling for a plan. The letter stated: "Also, amounts were improperly reimbursed to Mr. ______ for excessive numbers of long distance telephone calls made during meetings. These calls would appear to have no purpose related to Fund business." As a point of information, the number of challenged phone calls ranged from eight calls during a five-day meeting to 46 calls during a three-day meeting. The median were 18 to 25 phone calls during a three day meeting.

See comments in Q&A 10 regarding phone and cell phone expenses.

12. May a plan reimburse any recreational expenses while a trustee or plan employee is traveling on plan-related business?

Recreational expenses are personal expenses. A plan may not reimburse recreational expenses of any kind, including but not limited to golf, tennis, concerts, plays, shows, theme park admissions, museum fees, in-room movies, movies in a theatre, or movies on a plane. Recreation does not involve the administration of the plan even if plan business is discussed during the recreational activity. In addition, a trustee or plan employee may not be reimbursed for recreational expenses he or she has paid for anyone else such as a union official or employer representative. Based on several court cases, a plan service provider may not pay for the recreational activities of plan fiduciaries. These were found to involve party-in-interest transactions which are prohibited under ERISA. *See* discussion in Q&A 28.

13. In general, whose meeting expenses may be reimbursed by a plan?

A plan may reimburse expenses for those trustees and plan employees whose attendance is reasonably required at the meeting. Service provider expenses for attendance at a meeting may be reimbursed if such reimbursement is part of the contract with the service provider. Agreeing to reimbursement of expenses for a service provider must be justified on the basis of reasonableness; that is, it must be shown that such a contract provision was reasonable in view of the practices in the industry, and the fees charged are reasonable in relation to the services provided. *See* Q&A 9 concerning service provider compensation issues.

If the attendance of a trustee, plan employee, or service provider is not reasonably required for an entire meeting, he or she may only be reimbursed for expenses associated with the portion of the meeting for which his or her attendance is reasonably required. For example, if someone stays at a hotel for an entire multi-day meeting and only participates in the meeting for part of a single day, the plan should not reimburse that person's hotel and other expenses for the entire meeting.

In one recent investigation, the DOL determined that it could be a prohibited transaction for the plan to provide meals to service providers attending meetings. (In some cases, the contracts of the service providers did not include reimbursement for expenses. Therefore, meals were not part of the provider's agreed upon compensation.) The DOL determined that not all providers may be required to attend the entire meeting and, in such case, the provision of meals may not be reasonable compensation. The DOL stated that trustees must consider whether providers are required to attend the entire meeting, and "examine the agenda, the total compensation already paid to the service providers and all other facts and circumstances necessary to determine that the payment for a service provider's meals is a necessary part of his compensation and not a prohibited transaction."

14. May a plan pay or reimburse expenses associated with spouses, family members, or friends?

Under no circumstances may a plan pay or reimburse expenses for spouses, family members, friends or colleagues who accompany a trustee or plan employee on plan business. This includes, but is not limited to, the cost of meals paid for by a plan or a service provider, airfare, and incremental increases in lodging costs. Such expenses do not involve the administration of the plan.

A plan should not advance expenses for these individuals even if they are to be reimbursed later as this may be construed as a loan by the plan to a party-in-interest. Such a loan would be a prohibited transaction in violation of ERISA §§406(a)(1)(B) and 406(b)(1) and (3).

We were advised that, in one case, the DOL disallowed the cost of meals for spouses of attendees at a recognition dinner held in conjunction with an apprenticeship and training fund contest. We were also advised that the DOL disallowed the expenses associated with the attendance of service providers and union representatives at a plan's Christmas party (however, the DOL did not challenge the party itself).

Service providers should not pay expenses for spouses, family members, friends or colleagues of a fiduciary, or any other personal expense of a fiduciary. Such payments have been found to be a violation of ERISA §406(b)(3). In DOL investigations, the fiduciaries who have received personal expenses from a service provider have been required to reimburse such amounts with interest. Some court cases have also found a violation when service providers pay such expenses. *See* Q&A 28 and particularly *Brink v. DaLesio,* 496 F. Supp. 1350 (D. MD. 1980) and *Secretary of Labor v. Carell,* 17 EBC 1159 (M.D. Tenn. 1993).

Recent Voluntary Compliance Letters make it clear that it is the Department's position that a fiduciary's receipt of a personal expense from a service provider was imprudent under ERISA. This is true in one case even where the fiduciary had understood the expense to be a legitimate educational expense but the DOL found it to be personal under the circumstances. DOL takes the position that the receipt of a personal expense from a service provider constitutes self-dealing violations of ERISA and violates the anti-kickback rule, ERISA §§406(b)(2) & (3), whether or not the fiduciary realizes the expense is personal.

In one case, clarification was requested from the Department as to whether the plan could seek recovery from the service provider rather than from the fiduciary who unwittingly received the deemed personal expense from the service provider. The Department stated its position that since the fiduciary received the questioned expense (which the Department characterized as a "kickback"), he was responsible for the repayment to the plan. The Department also stated its opinion that to solicit or allow the service provider to repay the plan on behalf of the fiduciary would constitute additional self-dealing violations of ERISA.

See Q&A 28 for further information concerning payment of expenses by service providers.

15. May a plan pay or reimburse expenses for anyone else not associated with the plan?

A plan may not reimburse a trustee or plan employee for expenses paid by them for anyone not associated with the plan. This includes, but is not limited to, union officials and employer representatives. If the expenses would not be reimbursed if the other person sought reimbursement directly from the plan, a trustee or plan employee may not be reimbursed by the plan for paying those expenses. *See* Q&A 14 concerning expenses for spouses, family members or friends.

A common practice at conferences is for one trustee to pay for a meal for a trustee of another plan and, in exchange, the trustee of the other plan later pays for a meal for the first trustee. Neither trustee may be reimbursed for the meal expense of the trustee of the other plan. The DOL has specifically addressed this in investigations. These are not expenses of the plan of the paying trustee.

We understand that the DOL also has challenged a plan fiduciary who paid for and was reimbursed for meals of other fiduciaries of the same plan. Apparently, the basis for this position is that the paying trustee did not incur the expenses of the other trustee in the performance of the first trustee's duties. This would mean that trustees of the same plan eating together would be required to get separate checks at restaurants, which is not always possible. We believe this is largely a concern about documentation and that this practice is unlikely to be questioned if the receipt clearly shows the number of entrees and the individuals at the meal are contemporaneously documented.

16. May a trustee or plan employee receive reimbursement for travel expenses for days other than the days attending a meeting?

The DOL has challenged and disallowed trustee expenses in some cases involving multi-day meetings because trustees or plan employees may only receive reimbursements for days during which they are actually in attendance at a meeting and, when appropriate, the day before and the day after the meeting as needed for travel. The DOL position is that if a conference ends early enough in a day that the trustee or employee would be reasonably able to return home that same day, expenses for the next day should not be reimbursed. This would generally only apply to a conference or a meeting for which the ending time was known when the travel arrangements were made. It may be difficult to arrange to return the same day if a meeting unexpectedly ends early. Meetings should not be arranged to stretch out over a longer time period than reasonably necessary to conduct the business of the meeting.

If a meeting or conference starts late enough in a day that the trustee or employee would reasonably be able to arrive that same day in time to attend the meeting, expenses for the previous day should not be reimbursed.

However, if the trustee or plan employee can provide specific documentation that the total expenses of extra days would be less than the expenses for the time period discussed above, the trustee or plan employee may be reimbursed for the extra days that produce the savings. Otherwise, extra days involve personal expenses since the extra time and expenses were not "properly and actually incurred" by the fiduciary in the performance of his duties for the plan.

This issue has been raised by the DOL in several investigations. In one investigation, the DOL came very close to stating that the "Saturday night stay-over rule" was improper. Under this rule, which is common in many plans' expense policies, a trustee or plan employee may be reimbursed for the expenses of staying over a Saturday night (either before a meeting starts or after it ends) if, by doing so, they secure savings on airfare that exceeds the expenses incurred. Ultimately, the DOL did not take the position that the rule was *per se* improper. The DOL stated its opinion that reimbursement of the expenses associated with the Saturday night stay is permissible as long as there is a net savings to the plan and the additional expenses are determined to be reasonable when considering all of the facts and circumstances. The DOL stated that the fiduciary approving the Saturday night stay-associated expenses must carefully examine the expenses to determine if it is prudent for the plan to allow the reimbursement when considering all of the facts and circumstances.

We were advised that, in two investigations, the DOL took the position that the fiduciary must document that the money saved on the Saturday night stay-over fare was greater than the cost of the hotel accommodations and meal expenses. The DOL wanted written documentation of what the airfare would have been if the Trustee had traveled to the meeting on a Sunday instead of the actual airfare incurred by traveling on Saturday.

We were also advised that this issue was not raised in several investigations even though the plan expense policy included reimbursements for Saturday night stay-overs.

At a minimum, a fiduciary or plan employee seeking reimbursement for expenses associated with extra days must submit specific documentation that the additional days resulted in a net savings to the plan.

The Saturday night stay-over rule originated when airfares were structured to give considerable discounts for staying at a destination over a Saturday night. This is no longer always the case. In fact, the differential in airfares seems to be related to how far in advance the fares are booked and whether the fare is restricted or unrestricted. Some savings can often be realized by staying over a Saturday night but often the savings are not sufficient to cover the expenses associated with the additional days. The documentation submitted to support the stay-over-related expenses should not compare air fares from different time periods or different classifications. For example, the air fare without a stay-over used as a comparison should be obtained at the same time as the booked airfare. If the stay-over airfare is a restricted airfare, the comparison airfare should also be a restricted airfare. The DOL has not required fiduciaries and plan employees to always book restricted airfares, presumably because the person traveling may not be able to travel at the time of the available restricted fares or may be required to change reservations. However, if the restricted fare would have served the traveler's needs for travel with a Saturday night stay-over, it would have presumably met the traveler's needs for travel without the stay over. If there is some reason that this is not the case, that reason should be presented with the documentation.

Additional travel days may also be required if a plan fiduciary or employee travels by train, bus, or car. In this situation, it is common for plan expense policies to cap the total expenses associated with travel by train, bus or car by the amount of regular coach airfare. The amount of the airfare that is used as the measure must be documented.

17. Where may plan meetings be held?

If those attending a plan meeting travel from different parts of the country, there is no specific meeting site that must always be favored. However, in selecting sites, plan fiduciaries must be mindful of the relative costs of various locations. The trustees do not have to select the least expensive locations, but a comparison of the costs of a proposed meeting site with the costs of a meeting at the plan office should be considered. The selection of a resort area in high season at an expensive site could be called into question as not reasonable. Similarly, the meetings should not be held at an unreasonably expensive hotel nor should meals be at the most expensive restaurants. Meetings should not be held outside of the country if to do so would incur expenses in excess of meeting at a reasonable location within the U.S. However, meeting outside of the country or at any location is not *per se* improper. Whether an expense is reasonable must be considered under all the facts and circumstances. DOL Reg. §2550.408c-2(b)(1).

If those who will be seeking reimbursement of expenses from a plan are located within a single region or city, the meeting should be held in that region or city, unless there is some reason to benefit participants and beneficiaries that the meeting must be held elsewhere and this reason is documented by the plan fiduciaries. For example, in one case brought by a participant, a court determined that it was not a breach of fiduciary duty for a board of trustees based in Virginia to hold a meeting in conjunction with the IFEBP Annual Conference even when that conference took place in Hawaii. *See King v. Guyan*, 1992 Dist. Lexis 21582 (E.D. Va. 1992). The DOL was not party to that suit and would not consider itself bound by the result.

In a 2005 investigation, the DOL took the position that it was imprudent to hold trustees meetings in connection with IFEBP meetings since this required the plan to pay for the travel expenses of plan professionals who would not have been required to travel at plan expense if the meetings were held at the plan office. The DOL concluded that these expenses were not reasonable and necessary expenses of plan administration, were imprudent and excessive. The payment of these expenses were prohibited transfers of plan assets to or on behalf of fiduciaries in violation of ERISA §406(b)(1), or prohibited transfers of plan assets to parties-in-interest in violation of ERISA § 406(a)(1)(D).

18. May a trustee or plan employee receive reimbursement for first class or non-discounted airfares or train fares?

In general, a trustee or plan employee does not have to find the lowest airfare or train fare. In the first place, it can be extremely difficult to determine the lowest fare due to various sales, special rates and internet fares. A plan trustee or employee may not be able to make the reservation far in advance because other obligations around the time of the travel are not yet known. In addition, deeply discounted fares may be available only at inconvenient times, and it would not be reasonable to require trustees to travel at those times. Non-discounted coach fares should also not be taken if under the circumstances a discounted fare is reasonably available. It is often less expensive to book a restricted fare and pay a $100 change fee than to fly on an unrestricted fare. Therefore, if a restricted fare is booked, the change fee can generally be reimbursed.

The plan should reimburse only the actual fare for the trustee or employee to the extent the fare is reasonable under the circumstances. A plan cannot reimburse the amount it would have cost to purchase a ticket if the trustee or employee travels on a free ticket since that amount is not actually incurred as required by ERISA §408(c)(2).

Unless there are unusual circumstances which must be documented, we believe DOL would not consider first-class airfare to be reasonable. Although many believe DOL would approve first-class airfare for travel in excess of a certain time such as three or four hours, we found nothing affirmative to indicate that this is true. In fact, we found no instance in which the DOL affirmatively approved first-class airfare. For instance, in a Voluntary Compliance Letter the DOL required the plan to amend its expense policy to eliminate first-class airfare. We have been advised that DOL has not challenged first-class airfare in some investigations where there was a good reason such as the large size of the person traveling and/or the long distance involved.

If the plan's reimbursement policy allows for first-class airfare, documentation of the circumstances under which first-class travel would be permitted and the reasons why the approving fiduciary determines it to be appropriate would be helpful in a DOL investigation.

19. May a trustee or plan employee receive reimbursement for cab fare or the cost of a rental car?

In general, a plan may reimburse the expenses of a rental car, but only to the extent a car is reasonably needed for travel. For example, if the meeting or conference is held at a hotel adjacent to the airport, a car would not be needed. If the cost of taxis would be less expensive, a rental car should not be used unless several people attending the meeting can share the car, the cost of the car would be less expensive than multiple taxis fares, and this fact is documented. However, we were advised of one investigation in which the DOL disallowed the expenses of the rental vehicle where the trustee rented a larger vehicle and transported several other trustees.

We were advised of one investigation in which the DOL disallowed a portion of the cost of the rental car finding that mileage in excess of the mileage to and from the airport was personal.

A trustee or plan employee does not have to secure the lowest priced rental car. However, the DOL has taken the position that a plan may not reimburse for the use of a rental car for days in excess of the days for which expenses can be reimbursed or for the fees incurred when additional drivers are added to the rental contract.

Cab fare to and from the airport is permissible. However, in one case an expensive cab fare to a restaurant far from the hotel was found not to be reasonable when there were many restaurants to choose from within a reasonable distance from the hotel.

20. May a plan pay or reimburse transportation expenses in the vicinity of the plan?

In general, trustees and plan employees may be reimbursed for mileage (for the use of a personal vehicle) and parking incurred while on plan business, including mileage to and from the site of a meeting in the home city or area or cab fare if there is some reason that the individual cannot drive. However, if the mileage involves a person's regular commute, mileage and parking should not be reimbursed. Car rentals in an individual's home city would almost always be inappropriate. Service providers may be reimbursed transportation expenses in the plan's home city if their contracts with the plan provide for such reimbursements.

In some circumstances, a car is part of the compensation package of a plan employee. If this is the case, the terms of the arrangement must be documented and must be approved by the trustees. If the package also includes such items as gas, repairs and a rental car while repairs are ongoing, these terms must be documented. Such items will be considered part of the overall compensation package of a plan employee which must be reasonable. *See* Q & A 5 concerning compensation terms for plan staff.

21. May a plan pay for, or reimburse the expense of, alcoholic beverages?

In general, a plan may not pay for or reimburse a trustee or plan employee for the expense of alcoholic beverages. However, under the facts and circumstances approach, if a trustee or plan employee has a glass of reasonably priced wine or other alcoholic beverage with dinner, DOL may not challenge the expense. However, bar bills were disallowed in several investigations and were challenged in one suit filed by DOL.

22. May a plan pay or reimburse the cost of trustee or plan employee meals while the trustee or plan employee is traveling on plan business?

A plan may pay the reasonable cost of the meals of trustees and plan employees while traveling on plan business. The plan may pay for the meals of service providers if the contract with the service provider includes reimbursement for meal expenses and the expenses are reasonable. A meal expense might not be considered reasonable if it was incurred after the fiduciary or plan employee has completed his or her performance of duties for the plan. For example, absent special circumstances, the plan could not reimburse for the expenses associated with a dinner after a meeting ended when the individual lived in the area or after a traveler had returned to his or her home city. *See* Q&A 23.

23. May a plan pay for the cost of meals for a trustee, plan employee or service provider in the vicinity of the plan?

A plan may not pay the expenses of meals that do not involve any plan business. For example, it may be acceptable to hold a meeting at a restaurant if plan business is transacted during the meal (*see* example below) but in two separate cases the DOL found that it was not acceptable for the plan to pay for a meal after the meeting was over. The plan may also pay for reasonably priced lunches that are brought into the meeting if the meeting continues through lunch. Local meals for service providers should only be paid for by the plan if the attendance of the service provider is required during the part of the meeting that is held during the meal.

We believe that service providers may pay for the meals of trustees, plan employees, or other service providers, if the plan itself could pay for the meals. If the plan itself could not pay for the meal, either because the meal was not involved with the performance of duties for the plan or because the amount of the meal expense was unreasonable, the expense or the excess portion of the expense might be considered a personal expense and a service provider's payment of the expense might be considered a violation of ERISA §406(b)(3). We have not found affirmative support for this position in a DOL Opinion or court case.

We were advised of one investigation in which the DOL found that the practice of the plan's co-chairs and administrator having lunch once a month to review the upcoming agenda and other issues that arose between meetings was improper. The DOL stated that since all were local, the meetings could be held in the plan office and not at a meal time. The DOL ultimately yielded to the argument that the co-chairs had other jobs and this was one of the most convenient times to meet. The costs of the lunches were also extremely modest.

In a 2005 investigation, the DOL challenged the cost of monthly meetings for plan subcommittees as well as the costs of the annual dinner held in the month of December. We were advised that the investigator had shown no flexibility in response to the plan's argument that these meals were part of the plan's business. DOL was demanding reimbursement of meal costs for six years.

24. May a plan pay or reimburse the expenses of trustee or plan employee lodging while the trustee or plan employee is traveling out of town on plan business?

A plan may pay the reasonable expenses of lodging for trustees and plan employees while traveling out of town on plan business. The plan may pay for the lodging of service providers if the contract with the service provider includes reimbursement for lodging. The rate should not exceed a comfortable and safe but not extravagant hotel reasonably convenient to the location of the meeting or conference. We are aware of instances in which DOL investigators challenged hotel expenses arguing that the hotel rate paid by the trustees should not exceed the rate at which government employees could be reimbursed under government *per diem* guidelines, but we are not aware of any instances in which the DOL successfully pursued reimbursement for the excess amounts, perhaps because of the facts and circumstances of individual cases.

In a 2005 investigation, the DOL took the position that staying in a hotel designated as the "best" hotel accommodations at the IFEBP Conference rather than the "standard" hotel accommodations was prohibited by the plan. This was based on the wording of the plan's expense policy that provided for reimbursement of the prevailing rates for the conference.

25. May a plan pay for the expenses of lodging for trustees or plan employees who live in the area where a meeting or conference is held?

Absent unusual circumstances, a plan may not pay for the lodging of trustees, plan employees, or service providers who live near the location of a meeting or conference. In a Voluntary Compliance Letter, the DOL determined that it was not proper for the plan or a service provider to pay the expenses of a fiduciary to stay at a hotel in the city during a conference when the fiduciary lived approximately an hour from the meeting location but had not presented evidence that the meeting started unusually early or ended unusually late or that there were other circumstances requiring the stay in the hotel.

26. May a plan pay for the attendance by the trustees or plan employees at any events sponsored by the union, an employer, or other organization?

A plan may not reimburse expenses connected to the attendance of a plan fiduciary or employee at union or employer events, or at any other event (except for educational conferences), at which no plan business is transacted. Plan fiduciaries, employees or service providers may attend union and employer meetings to perform educational functions, provided the costs and materials associated with such attendance are reasonable and provided the plan does not pay or reimburse the union or employer for any of their expenses associated with the meeting. Documentation of the plan-related reason for attendance would help in an investigation.

27. May a plan pay the expenses for trustees, plan employees and service providers to attend educational conferences?

A plan may reimburse the expenses for trustees and plan employees to attend educational conferences addressing topics that are associated with their duties for the plan. Offers to attend a conference, meeting, or other event at the expense of a service provider should be refused unless the expenses of attendance could be reimbursed by the plan itself, i.e., the expenses must be reasonable and not constitute a personal expense. Even if the plan could pay the costs of the conference, we know of instances in which the payment by the service provider was questioned by DOL.

A plan may not pay the expenses of the general professional education of its service providers. The DOL has required service providers to reimburse the plan for expenses paid by a plan for general education. However, we believe that a plan could pay the expenses of a service provider to attend a conference if the plan directed the provider to attend the conference to gain specific knowledge or information for the plan. The determination by the plan that the provider should attend the conference and the expected benefit to the plan and its participants should be documented. Expenses would be paid in accordance with the service provider's contract.

We were advised that, in one investigation, the DOL disallowed late registration fees for attending an educational conference.

28. May a service provider pay expenses of a trustee or plan employee?

Court cases have held that a service provider cannot pay for personal expenses such as extra days at hotels, meals for spouses, or entertainment and recreation (including but not limited to golf or tickets for games, massages, shows and sporting events). Also, trustees and plan employees should not accept gifts from a service provider. Trustees and plan employees should not accept items such as reduced or waived banking fees, personal investment advice, use of a condo or vacation property, or free airfares and vacations. Payments by a service provider of personal expenses are prohibited transactions. ERISA §406(b)(3).

The following cases address, among other things, situations in which payments were made by service providers of gifts and gratuities to plan fiduciaries were held to be illegal under ERISA or where service providers gave a "thing of value" to plan fiduciaries and that action was held to violate ERISA. Although in most cases the circumstances were pretty egregious, the cases also addressed relatively small items of entertainment. *Lowen v. Tower Asset Management*, 829 F.2d 1209 (2d Cir. 1987), *aff'g* 653 F. Supp. 1542 (S.D.N.Y. 1987); *Brink v. DaLesio*, 496 F. Supp. 1350 (Dist. MD 1980); *Secretary of Labor v. Carell*, 17 EBC 1159, (Middle Dist. Tenn. 1993); *Whitfield v. Tomasso,* 682 F. Supp. 1287 (E.D.N.Y. 1988); *Donovan v. Tricario*, 1984 U.S. Dist. Lexis 17516

Two cases-- *Brink v. DaLesio*, 496 F. Supp. 1350 (Dist. MD 1980) and *Secretary of Labor v. Carell*, 17 EBC 1159, (M. D. Tenn. 1993)--are particularly worthy of discussion. We have quoted the relevant passages at length and added emphasis to certain statements because we feel that the court's own words are instructive.

In *Brink v. DaLesio*, 496 F. Supp. 1350 (Dist. MD 1980) the court discussed the meaning of ERISA § 406(b)(3) at length:

> The proper interpretation of this provision [ERISA §406(b)(3)] has been the subject of controversy in the instant case. An examination of the legislative history indicates that it was designed to prevent kickbacks. *See* H.R. Conf. Rep. No. 93-1280, 1974 U.S. Code Cong. & Admin. News 5038, 5089. *See also* Little and Thrailkill, Fiduciaries Under ERISA: A Narrow Path to Tread, 30 Vand. L. Rev. 1, 25 (1977). The controversy in this case under both ERISA and the common law centers around the issue whether the plaintiffs need show that there was a *quid pro quo* for the gratuities or that harm to the union or the Funds resulted. ***There is neither case law nor regulations governing the proper interpretation of §1106(b)(3); nevertheless, an examination of decisions construing other provisions of ERISA demonstrates that plaintiffs need not show that the receipt of gratuities actually influenced DaLesio's discharge of his fiduciary duties.*** *[Emphasis added.]* Initially, it should be noted that ERISA is a "comprehensive remedial statute designed to protect the interests of participants in employee benefit plans" and that a broad construction of the statute is therefore appropriate. *Marshall v. Kelly,* 465 F. Supp. 341, 349 (W.D. Okla. 1978). ***Therefore, "the question of whether ERISA has been violated does not depend on whether any harm results from the transaction. Congress was concerned in ERISA to prevent transactions which offered a high potential for loss of plan assets or for insider abuse.… "*** *[Emphasis added.] Id. at 354*. A similar approach was taken by the court in *Gilliam v. Edwards*, (Slip Op.) (D. N.J. June 9, 1980) in construing §1106(b)(1) barring a fiduciary from "deal[ing] with the assets of the plan in his own interest or for his own account." ***The court noted that a defendant who engages in a prohibited transaction does not escape liability by showing "the absence of bad faith, or…the presence of a fair and reasonable transaction.… "*** *[Emphasis added.] Id.* A strict construction of the prohibited transaction provisions is also justified by administrative convenience. ***In addition, the court noted that it is psychologically unrealistic to expect a trustee to ignore his personal interests when they are potentially at odds with his fiduciary obligations.*** *[Emphasis added.] Id.*
>
> The defendant has argued that the statutory language dictates the opposite result. The Court is in agreement that the provision, standing alone, is not unambiguous. It would appear to require the plaintiff to show that the defendant received consideration in a transaction in which the plan assets were involved. ***In other words, it might be argued that the language suggests that a showing of an actual effect on the plan is required. Such an interpretation, however, would render the provision superfluous in light of §1106(b)(1) and (2) which clearly prohibit self- dealing with plan assets and representation of parties with adverse interests in transactions involving plan assets*** *[emphasis added]****.*** In addition, the defendant's suggested interpretation is inconsistent with the common law rule that a *quid pro quo* need not be shown, *see, e.g., United States v. Bush*, 522 F.2d 641, 648 (7th Cir. 1975); *McGinnis v. Roger*, 262 Md. 710, 732 (1971). ***Rather, "a trustee …is not permitted to place himself in such position that the interest of***

> ***the beneficiary and his own personal interest do or may conflict; and the question of whether or not such a position has resulted in a benefit or loss to the beneficiary is not to be inquired into*** *[emphasis added]*. **"** *Mangels v. Tippett*, 167 Md. 290, 300 (1934). ***In light of these considerations, then, the Court has determined that §1106(b)(3) is violated when a fiduciary receives gratuities from any party dealing with the Fund*** *[emphasis added]*.

In *Secretary of Labor v. Carell*, 17 EBC 1159, (M. D. Tenn. 1993), the court found that the trustees of the plans breached their fiduciary duties by accepting payment of airfare, lodging, meals, refreshments, entertainment and hotel expenses from a provider of administrative services. The payments covered trustees' expenses as well as the expenses of their wives. Again, the courts own words are worthwhile:

> Defendants themselves have admitted to providing the payments and reimbursements to the trustees and would have this court assign a label of goodwill to them. These goodwill offerings were undoubtedly within the scope of Congress' concern when it enacted ERISA.
>
> Defendants also argue that the value of the gratuities in question are too insubstantial to trigger a presumption of illegal kickback (*quid pro quo*) and that the Secretary has not supplied evidence to show that the gratuity was made in connection with a transaction involving plan assets.
>
> ***Defendants point to nothing in the statute or its legislative history that supports their assertion that the courts must look to the amount in controversy when applying §1106(b)(3). Indeed, none of the cases cited by defendants advance this proposition. While it is true that the majority of the cases cited by the Secretary involve well established cases of illegal kickbacks of substantial dollar amounts, it does not logically follow that insubstantial amounts are outside the coverage of this provision*** *[emphasis added]***.**

Citing the *Brink* case, the *Carell* court held that the finding of a §406(b)(3) violation does not require proof of actual harm to the plan resulting from the prohibited transaction.

> The court found that the trustee, DaLesio, violated ERISA although the amount in controversy was accounting services valued at only $500.00. "Receipt of gratuities . . ." said the court, "violated DaLesio's duties under . . . ERISA without regard to whether the costs attributable to those services were passed on to the . . . Fund and without regard to whether there was any demonstrable effect on DaLesio's discretion concerning the selection and retention of accountants to perform services for those entities." *Id.* at 1368. ***This amount, under defendants' theory would be insufficient to give rise to a presumption of impropriety. Sound logic, the intent of the statute and sound policy militate against the adoption of defendants' position*** *[emphasis added]*.

In *Lowen v. Tower Asset Management, Inc.*, 829 F. 2d 1209, 8 EBC 2457 (2d Cir. 1987), the court stated that "a fiduciary charged with a violation of Section 406(b)(3) must either prove by a preponderance of the evidence that the transaction in question fell within an exemption,…or must prove by clear or convincing evidence that compensation it received was for services other than a transaction involving the assets of a plan." *Id.* at 2462. The court commented that any doubt about a causal connection between payments to a fiduciary and the investment or expenditure of plan assets should be resolved against the fiduciary. *Id.* at 2462. The requirement that for a §406(b)(3) violation the fiduciary must benefit personally "in connection" with a transaction involving plan assets actually moderates the strict common law rule that a trustee may not profit (other from its fees) from transactions involving trust assets. *See Restatement (Second) of Trusts,* §170(1) (1959). However, the Court of Appeals in *Lowen* commented that the "in connection" with requirement "should not be construed in a way that creates a loophole that permits self-dealing and, in particular, "kickbacks" to fiduciaries." *Lowen* at 2462.

Taken together, these three cases stand for the proposition that for a violation of ERISA §406(b)(3)--

- There need be no showing that the receipt of gratuities actually influenced the trustee in the discharge of his fiduciary duties.
- There need be no showing of harm to the plan.
- The fiduciary who receives gratuities does not escape liability by showing the absence of bad faith, or the presence of a fair and reasonable transaction.
- The receipt of even insubstantial amounts of gratuities violate §406(b)(3).
- The fiduciary receiving the payment bears the burden of showing that an exemption applies or that the payment was not "in connection" with a transaction involving plan assets.

Since ERISA §406(b)(3) prohibits a plan fiduciary from receiving any consideration for his own personal account from any person dealing with the plan, we believe that a service provider may pay the expenses of a trustee or plan employee if it would be permissible for the plan to pay those expenses directly. If the plan could pay the expenses (i.e., they are the types of expenses that the plan may lawfully pay or reimburse and are reasonable), they are not personal expenses. However, we have not found affirmative support for this position either in DOL opinions or court cases.

One case stated in *dicta* that ERISA fiduciaries should not be held liable for accepting a token gift from a service provider but then went on to find that the gift alleged in the case at issue was not a token gift. *See Ossey v. Marolda*, 1999 U.S. Dist. Lexis 14293 (ND Ill).

We are aware that an investment professional was investigated by DOL and was advised that paying for dinners not associated with business, tickets, golf and other personal expenses was a prohibited transaction. The consultant was directed to cease such activities.

We believe, however, that a general client reception for all clients of a service provider may be viewed differently by the DOL than entertainment directed specifically to the fiduciaries of one plan.

<u>Criminal Violations:</u> The receipt of gifts and gratuities may also constitute a criminal violation under 18 USC §1954. *See U.S. v. Kirkland,* Dist. Ore. CR 02-350-BR (2004); *U.S. v. Rosenthal*, 9 F.3d 1016 (2nd Cir. 1993); *U.S. v. Romano*, 684 F.2d 1057 (2nd Cir. 1982); *U.S. v. Friedland*, 660 F.2d 919 (3rd Cir. 1981); *U.S. v. Soures*, 736 F.2d 87 (3rd Cir. 1984); *U.S. v. Robilotto*, 828 F.2d 940 (2nd. Cir 1987); *U.S. v. Schwartz*, 785 F.2d 673 (9th Cir. 1986).

U.S. v. Kirkland is a relatively recent case and the court reaches a conclusion concerning the application of 18 USC §1954 that is different in some respects from the results in earlier cases. The earlier cases specifically rejected the need to prove a *quid pro quo.* To obtain a conviction, the government had only to show that the person who received the gratuity was in the real or apparent position to influence a plan's action. The court in the *Kirkland* case took a different position based on the decision of the U.S. Supreme Court in *U.S. v. Sun-Diamond Growers of California,* 526 U.S. 398 (1999), a case involving gifts and gratuities to a public official. In the *Sun-Diamond* case, the Supreme Court held that a clear linkage must be shown between the gifts given and the action taken.

The court in *Kirkland* found that the government must prove that a substantial factor in the service provider's motivation to give a thing of value was the trustee's specific past or anticipated actions or decisions. It is not enough that the service provider is motivated merely by a trustee's general capacity to decide matters that affect the service provider's business interests or if the service provider sought merely to build a reservoir of goodwill. Nevertheless, the court found the service provider guilty on 12 counts where the government's case met the standard of proof. Interestingly, the court did not find the trustee guilty of illegally accepting gratuities. The evidence was not sufficient for a criminal conviction but did establish a breach of fiduciary duty.

Although it is a very common practice for plan service providers to pay for or provide entertainment or other expenses for plan fiduciaries and employees, plan fiduciaries should understand that this may constitute a prohibited transaction under ERISA §406(b)(3) or even a criminal violation under 18 USC §1954. It has been our experience, as well as being apparent from recent investigations and court cases, that the government intends to pursue both plan fiduciaries for gratuities received from service providers and the service providers themselves.

<u>Fiduciary Duty to Disclose Attempts by Service Provider to "Influence" Trustee:</u> Further evidence of the DOL's negative views on entertainment and other benefits from service providers came at a 2005 conference in which a representative of the DOL discussed a recent Information Letter issued by the Department. The Information Letter was dated February 23, 2005 and concerned the conduct of a trustee involved in a selection process for a service provider. It is available at www.dol.gov/ebsa/regs/ILs/il022305.html. The letter was issued in response to a request for guidance from the Trustee involved.

The Trustee requesting the Information Letter from DOL served as a Union Trustee of a multiemployer plan. In his personal capacity, he was elected to the county legislature and, when the events addressed in the Information Letter occurred, he was running for re-election. At the time of the campaign, the fund on which he served as Trustee was in the process of a search for a third-party administrator (TPA). Condensing the facts, which are useful to read, both candidates for TPA as well as other existing service providers of the fund were solicited by the re-election committee to contribute to the campaign and did, in fact, contribute. There is no evidence that the trustee was involved in this solicitation and when he discovered that the contributions had been made, the full amount of the contributions of both the potential and existing service providers was returned. In addition, the trustee recused himself from the final vote on the selection of the TPA.

Responding to questions at the conference, the DOL representative (commenting that his views were personal and may not represent the views of the DOL), noted that when a trustee is involved in a situation in which he may be conflicted, his recusal is sufficient to avoid a prohibited transaction. However, the Information Letter explains that the trustee may have an additional duty to advise the other fiduciaries that service providers gave him money. The reason for the disclosure is that the gifts by the service providers may indicate that they were trying to influence the trustee and the other trustees should know that these service providers were engaging in conduct which the DOL apparently thought was less than exemplary. When asked directly if this meant that each trustee must disclose to other trustees any time a service provider provided any benefit of a personal nature, the DOL representative said that it depends on the facts and circumstances. If there was a personal relationship between the two or a business relationship other than the fund, then the personal benefit might be for reasons other than an attempt to influence the trustee with respect to fund business. The position seemed to be that if the only relationship between the service provider and the trustee involved the fund, then the DOL interpreted the personal benefit as a possible intent to influence the trustee. Obviously, the Information Letter did not say this directly and the DOL representative at the conference may not have been stating the views of the Department. However, the comments should be taken into account, particularly in view of the resurrection of the LM-30/LM-10 reporting requirement.

<u>LM-3-/LM-10 Filing Requirement:</u> The filing of the LM-30 and LM-10 forms is a reporting requirement under the Labor-Management Reporting and Disclosure Act (LMRDA), not ERISA, and it is administered by DOL's Office of Labor-Management Services (OLMS), not the ERISA regulators in the Employee Benefits Security Administration (EBSA).

Since the initial announcement the DOL has issued detailed Q&A's concerning the LM-10 filing requirement[6] and has issued proposed regulations concerning the LM-30 requirements.[7] DOL has made significant efforts to answer questions and to post new Q&A's on the website as issues are addressed. The proposed regulations concerning the LM-30 filing requirement requested comments on many issues. Since comment was requested on the status of employee benefit plans as either "employers" or "businesses" for purposes of the LM-30/LM-10 requirements, DOL has noted that it will exercised its discretion not to enforce LM-10 reporting against employee benefit plans pending completion of LM-30 rulemaking.[8]

A review of the LM-30/LM-10 issues is beyond the scope of this paper. However, in connection with the issues addressed in this paper, and particularly in this Q&A 28, it is important to note that payments or things of value from a plan service provider must be reported on a union trustee's LM-30 report and must be reported by the service provider on its LM-10 filing. There is a *de minimis* exemption so that neither an LM-30 nor LM-10 filing is required for "insubstantial" gifts and gratuities or other payments or things of value. Currently, for the *de minimis* exemption to apply the aggregate annual value of gifts and loans, etc. from a single employer (*e.g.,* plan service provider) to a single union official may not exceed $250 and the amounts must be given under circumstances unrelated to the recipients' status in a labor organization.[9]

As discussed in this paper, we believe that under certain circumstances some such "economic benefits" are proper under ERISA and the fact that the LM-30 form seems to require reporting

[6] See http://www.dol.gov/esa/regs/compliance/olms/LM10_FAQ.htm
[7] Labor Organization Officer and Employee Reports; Proposed Rules, 70 Federal Register No. 166, pp. 51166-51225 (August 29, 2005).
[8] See Form LM-10-Employer Reports: Frequently Asked Questions, Q&A 73.
[9] See Form LM-10-Employer Reports: Frequently Asked Questions, Q&A 50.

them does not indicate that they are improper under ERISA or any other law.[10] However, as we have also indicated, some gratuities received by plan fiduciaries from service providers may constitute a prohibited transaction under ERISA §406(b)(3) or even a criminal violation under 18 USC §1954. We have become aware of a misunderstanding by some trustees that gifts and gratuities may lawfully be accepted from plan service providers up to the $250 annual *de miminis* exemption for the LM-30/LM-10 filing. THIS IS NOT CORRECT. The legal requirements under ERISA are separate from the reporting requirements for forms LM-30 and LM-10. We have learned from colleagues in two different DOL regions that DOL has requested (and has been given) records from plan service providers of entertainment, gifts and gratuities provided to trustees and has used these records in subsequent enforcement actions against the trustees. Because of the LM-10 filing requirement and the need to document the aggregate annual amount paid to or on behalf of each union trustee, service providers have detailed records of such expenditures. The ERISA rules apply equally to employer trustees.

The LM-30 filing requirement highlights the need to make certain that any benefit of any kind received from a plan vendor is in accordance with the requirements of ERISA. Trustees subject to the filing requirement should consult counsel on this matter and make certain that the appropriate records are available for the filing. Although we do not wish to imply that this is the only means of addressing this issue, we are aware of one plan that adopted a policy prohibiting service providers from giving anything of value to plan fiduciaries. A letter was sent to service providers stating:

> It is the policy of the ________ Funds that service providers to the Funds will not provide, directly or indirectly, anything of value of a personal nature to any individual Trustee or group of Trustees or their relatives including but not limited to any gifts, tickets, entertainment, charitable or other contributions, non-plan related lodgings or meals or good or services of a personal nature.

Such a policy would comply with ERISA; however, it appears that benefits from service providers permitted by such a policy and by ERISA would be covered by the LM-30 filing requirement unless they satisfied the *de minimis* exemption.

Information concerning the LM-30 filing requirement is available on the DOL website at http://www.dol.gov/esa/regs/compliance/olms/LM30factsheet.htm. A downloadable Adobe version of Form LM-30 along with instructions for completing the form is available on the Internet at http://www.dol.gov/esa/regs/compliance/olms/GPEA_Forms/blanklmforms.htm.

29. How should expenses claimed for reimbursement be documented?

A plan should have a written expense policy adopted by the trustees. In investigations, the DOL looks to the adopted expense policy to determine if the plan may pay or reimburse certain expenses. The policy may also be used to state the rationale for the plan's payment of certain categories of expenses. The policy should address many of the issues discussed in this paper.

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[10] The instructions to the LM-30 form state that "the fact that a particular financial transaction or interest is or is not required to be reported is not indicative of whether or not it is or is not subject to any legal prohibition; this must be tested by provisions of law other than those prescribing the reports."

All expenses should be individually itemized by date. The location and purpose of each expense should also be documented. Generally, there should be a written receipt for all expenses for which a receipt can reasonably be obtained. This is an item frequently addressed in a plan's expense policy and the policy must be followed. In a Voluntary Compliance Letter, DOL found that "generic" receipts and credit card billings alone are insufficient. The expenses must be itemized on the receipt.

It is very common for plan expense policies to provide that receipts are not required for reimbursement of expenses under $25. This is based on an old IRS rule and is for purposes of documenting deductions. The DOL does not necessarily follow this rule. DOL requires *documentation* of all expenses. However, in our experience in DOL investigations, DOL will accept documented expenses without receipts for amounts under $25 if the documentation appears believable. An expense without a receipt must be documented in the expense reimbursement request with information indicating the date, nature, purpose and location of the expense and who was present. *See McLaughlin v. Tomasso*, 9 EBC 2438 (E.D.N.Y. 1988)(trustees breached their fiduciary duty not only by incurring unlawful expenses but also by failing to monitor and keep adequate records of administrative expenses); *Dole v. Formica,*14 EBC 1397, 1407 (N.D. Ohio 1991) ("without some objective and contemporaneously recorded information, the Trustees could not evaluate the reasonableness of the compensation paid for the services received.").

We recommend that trustees not adopt an expense policy permitting reimbursement without receipts for amounts greater than $25. This encourages minimal documentation and raises the likelihood that expenses will be challenged by DOL in an investigation.

In connection with the documentation for payment of airfare, it is important to keep in mind that airline flights can be changed until the date and time of departure. Each change can generate a different ticket and related receipt. The fares for each ticket can differ significantly. The airlines do not require passengers to return tickets. Therefore, we have been advised that some plans have a policy of requiring trustees and plan employees to submit both the ticket and the boarding passes as documentation for air travel. These documents will substantiate that the ticket claimed as air travel was actually used, as a common ticket number is printed on each.

Finally, *see* Treas. Regs. §§1.274-5, 5A and 5T concerning substantiation requirements for tax purposes. These regulations do not control the substantiation of expenses for purposes of the fiduciary requirements of ERISA but may be useful in formulating documentation policies.

30. May a plan provide expense advances or *per diems*?

We are using the term "*per diem*" to refer to an amount paid to a plan fiduciary or employee by the plan that the plan fiduciary need not account for or reimburse. We are using the term "expense advance" to refer to amounts to be used only for expenses that the plan may properly pay. The expenses for which the advance was used must be documented as soon as possible after the meeting and the excess, if any, must be refunded to the plan.

As the DOL makes clear in Advisory Opinion 80-58A which addressed this issue, whether or not a "*per diem*" can be paid to a plan fiduciary is determined by whether the plan can compensate the fiduciary. *See* Q&A 3. The Advisory Opinion stated:

> In your letter, you ask whether, in view of the Department's adoption of regulations under section 408(c)(2) which do not contain an express reference to a per diem allowance, the Fund may continue to pay such an allowance to its trustees or whether it may reimburse them only for actual expenses incurred in the performance of services for the Fund.
>
> If the limitations in section 408(c)(2) on the receipt of compensation do not apply to a fiduciary, that section permits such a fiduciary to receive reasonable compensation from a plan for services rendered. In addition, section 408(c)(2) does not specify the manner in which such compensation must be determined, and, therefore, a plan may pay a fiduciary who is permitted to receive compensation from the plan a reasonable amount determined on a daily (or per diem) basis.
>
> Section 408(c)(2) also permits a plan to reimburse expenses incurred by a fiduciary in the performance of services for a plan, including expenses incurred by a fiduciary who also receives full-time pay from an employer or an association of employers whose employees are participants in the plan, or from an employee organization whose members are participants in the plan. However, reimbursement is permitted only for expenses that are properly and actually incurred. Therefore, because a fiduciary who is paid a per diem allowance as a means of reimbursement may receive an amount in excess of his actual expenses, such a method of reimbursement is not permitted under section 408(c)(2).
>
> However, … the Department's regulations under section 408(c)(2) permit a plan to pay an advance to a fiduciary to cover direct expenses to be properly and actually incurred, provided certain conditions are met. Therefore, in our view, a plan would not engage in a prohibited transaction solely because it advances funds to a fiduciary of the plan if, as provided in the regulation, the amount of the advance is reasonable with respect to the direct expenses that are likely to be properly and actually incurred by the fiduciary during the period covered by the advance, and provided that the fiduciary accounts to the plan at the end of such period for the expenses properly and actually incurred and refunds to the plan the amount, if any, by which the advance exceeds the fiduciary's actual expenses.

See DOL Regs. §2550.408c-2(b)(4).

It is very important that plan fiduciaries receiving expense advances account to the plan and refund any unused portion of the advance as soon as possible after the meeting or conference. Amounts not reimbursed for some period of time become an extension of credit to the plan fiduciary or employee and a prohibited transaction under ERISA §406(a)(1)(B).

The rules concerning *per diems* and advances may be summarized as follows:

- A plan fiduciary who <u>does not</u> receive full-time pay from certain parties-in-interest as discussed above and in Q&A 3 may receive either a *per diem* or an expense advance or both.
- A plan fiduciary who <u>does</u> receive full-time pay from certain parties-in-interest as discussed above and in Q&A 3 may <u>not</u> receive a *per diem* but may receive an expense advance.

- A *per diem* is compensation which must meet a reasonableness standard and must be approved by the trustees. A *per diem* need not be accounted for and any unused portion need not be reimbursed to a plan.
- An expense advance must be used only for the types of expenses that a plan can pay and that are reasonable in amount. A fiduciary who receives an expense advance must promptly account for the expenses to which the advance was applied and must reimburse any unused portion of the advance to the plan.

Conclusion

A plan's practices with respect to the trustee and plan expense issues discussed in this paper are generally reviewed by the DOL in the course of an investigation. It is important to understand the DOL's positions on these issues. It is also important to insure that plan fiduciaries and employees comply with ERISA's requirements that the required policies are adopted and proper documentation is provided regarding trustee and plan expenses. Although we have tried to collect the available information regarding the DOL position on proper trustee and plan expenses, this paper should not be read as providing definitive guidance about what the law is and what the DOL will do in a particular investigation or case. As previously noted in the introduction, the facts and circumstances applicable to each expense or fiduciary decision will significantly affect the assessment of whether or not the expense is proper under ERISA. In addition, we have found significant differences in the way in which DOL has treated certain issues. Certainly most of this is due to the underlying circumstances but to some extent it is also due to differences among individual investigators, different regional offices of DOL and differences between the field offices and DOL National Office. In consultation with their legal advisors, fiduciaries should use the information presented here along with other available information to evaluate their own practices, determine if they have any potential exposure and implement changes if deemed necessary. Our experience shows that simple changes concerning documentation of individual decisions and plan policies may make an enormous difference in the length, tone and ultimately the outcome of an investigation.

Updates; Request for Additional Information

We have learned a great deal in the process of preparing this paper from discussions with colleagues who reviewed earlier drafts. This has reinforced our view that it is important to exchange information and viewpoints concerning the issues addressed in this paper. We intend to update this periodically. Therefore, we request continued contributions of experiences from DOL investigations and/or the citation to relevant cases, opinions or regulations to make this project as complete as possible.