Office of the Comptroller of the Currency

Interpretive Letter #734, Part 2

Published in Interpretations and Actions August 1996

4. Duties of National Banks as Fiduciaries

Federal and state statutory and common law impose substantial duties and obligations on national bank trustees and managing agents in their relations with beneficiaries and accounts, including managing agency accounts. The fact that fiduciary funds are collectively invested does not diminish these fiduciary obligations. The obligations include duties of loyalty and care. Fiduciaries must act solely in the best interest of those relying on them to supervise their investments. Fiduciaries may not become involved in conflicts of interest that might affect recommendations made for their clients' benefit and must avoid even the appearance of impropriety in managing those funds. *See, e.g., Scott on Trusts* 170 (duty of loyalty), 172 (duty to keep and render accounts), 173 (duty to furnish information), 174 (duty to exercise reasonable care and skill) (4th ed. 1987); Cal. Prob. Code 16002 (duty of loyalty), 16004 (self-dealing); and Ill. Ann. Stat. ch. 760, para. 5/5 (duty of care).

OCC regulations also reinforce the substantial obligations to which national banks acting as fiduciaries are subject. National bank fiduciaries are prohibited from engaging in self-dealing, including investing funds "in stock or obligations of, or property acquired from, . . . organizations in which there exists such an interest, as might affect the exercise of the best judgment of the bank in acquiring the property . . . " 12 C.F.R. 9.12(a). This prohibition acts as a safeguard against bank fiduciaries speculating in trust property for their own benefit or putting their interests ahead of trust beneficiaries', and extends to transactions between a national bank and its affiliates. The prohibitions of section 9.12(a) do not apply, however, if the investment of funds in question is permitted by the trust instrument, court order, or local law. *Id*.

ERISA separately imposes significant duties on fiduciaries, including national bank managing agents, that make investment decisions for plans. ERISA defines "fiduciary" as a person who "exercises any discretionary authority or discretionary control" in managing plans "or exercises any authority or control" concerning management or disposition of the plan assets. 29 U.S.C. 1002(21)(A). That definition includes managing agents. The legislative history for ERISA confirms that Congress intended that *anyone* exercising management of plan assets would fall within the definition of "fiduciary". *See* H.R. Rep. No. 93-533, 93rd Cong., 2nd Sess., *reprinted in* 1974 U.S.C.C.A.N. 4639, 4648-4651. A national bank or bank affiliate acting as a managing agent ordinarily would have investment discretion and, therefore, a bank or bank affiliate acting in that capacity for a plan would be a fiduciary within the meaning of ERISA. *See* 12 C.F.R. 9.1(h).

ERISA requires fiduciaries to discharge their duties to plans "solely in the interest of the participants and beneficiaries and -- (A) for the exclusive purpose of: (I) providing benefits to participants and their beneficiaries". 29 U.S.C. 1104(1). The Bank must manage the Retirement Plans' investments in the Trust under a duty of care standard that requires the Bank to manage the funds entrusted to it with the same skill and care it would exercise if it were investing its own funds. *Id*. Those requirements help ensure that the Bank makes investment decisions solely to protect Retirement Plan participants' interests and to maximize the return on such interests. A fiduciary is subject to a duty of care in managing a plan's investments and must diversify the plan's investments to minimize the risk of large losses. If a fiduciary breaches its fiduciary duty to a plan, it is "personally liable to make good to such plan any losses to the plan resulting from each such breach . . ." *Id*. at 1109.

II. The Bank's Proposed Fiduciary Activities Are Not Proscribed by the Glass-Steagall Act

A. The Glass-Steagall Act and the Camp *Decision*

In its decision in *Camp*, the Supreme Court concluded that a collective investment fund marketed to the public violated the Glass-Steagall Act <**NOTE:** The Glass-Steagall Act was designed to separate aspects of commercial from investment banking. *See* 12 U.S.C. 24(Seventh), 78, 377, and 378. The sum effect of these restrictions is to limit the involvement of banks in certain activities, such as underwriting (where a bank commits to sell an issue, or some portion thereof, of new securities), that Congress considered to involve investment banking, and similarly keep securities firms from operating commercial banking businesses.> because, although the three activities involved in the proposal -- pooling trust assets, acting as managing agent, and purchasing stock for the accounts of customers -- were separately permissible for national banks, the combination of those activities created an investment vehicle that closely resembled a mutual fund. *Id*., 401 U.S. at 624-25. Such is not the case here, and the Glass-Steagall Act does not proscribe the Bank's proposed fiduciary activities.

In *Camp*, the OCC had approved a national bank's establishment of a collective investment fund to be marketed to persons investing a minimum of $10,000 and who authorized that bank to act as managing agent for such funds. The proposed fund was open to any retail customer without regard to the fiduciary purpose or tax-exempt status of the underlying assets. *Camp, supra*, 401 U.S. at 622, fn.8. Although the Supreme Court expressed concern about the combination of three separately permissible activities and investors' ability to freely redeem fund interests, the Court also indicated, however, that the combination of activities found impermissible in this instance could be permissible when a bank receives assets for a true fiduciary purpose and provides fiduciary services. The Court observed in *Camp* that the hazards the Glass-Steagall Act was enacted to avoid were "not present when a bank undertakes to . . . commingle assets which it has received for a true fiduciary purpose rather than for investment . . . . In short, there is a plain difference between the sale of fiduciary services and the sale of investments." *Id.*, 401 U.S. at 638. <**NOTE:** We also note that ERISA, and the fiduciary duties attributable to managing agents of retirement plans under ERISA, did not exist until 1974, after the Supreme Court's decision in *Camp*.>

The *Camp* court based its decision in part on a finding that the proposed activities could lead to various "hazards" associated with commercial bank participation in investment banking. The hazards included: 1) the loss of customer confidence due to losses on investments that customers purchased in reliance on the relationship between the bank and the funds; 2) the risk that a bank might support its securities affiliates with unsound loans; 3) the risk that the bank might make unsafe loans to companies in whose stock or securities the affiliate invested; 4) the temptation to make loans to customers to purchase securities of issuers whose securities the bank was underwriting; and 5) the conflict between the promotional interest of the commercial banker and the obligation of the commercial banker to render disinterested investment advice. *Id.*, 401 U.S. at 630-33, 636-638.

B. The Bank's Proposal, Involving a Fiduciary Activity, Does Not Implicate the Concerns Expressed in Camp

The Bank's proposal is materially different from the activities that the Supreme Court found violated the Glass-Steagall Act in *Camp* because the funds that the Bank would invest in the Trust would have the bona fide fiduciary purpose of promoting long-term retirement savings. The assets under Bank management would consist solely of Retirement Plan assets. By their very nature, these assets exist for a fiduciary purpose -- providing retirement income to plan participants. An individual participates in such a plan to guarantee or supplement, in the long-term, an income in his or her retirement years. The Bank would offer collective investment services only to tax-exempt Retirement Plans that serve as vehicles for retirement savings. The Bank already acts as managing agent for many of these Retirement Plans. Moreover, a participant may not redeem interests in the Trust without suffering a substantial tax penalty, subject to certain limited exceptions. The lack of redemption options helps ensure that the Trust operates according to its purpose, to accumulate funds to provide future retirement income for plan participants. *See*, *e.g.*, 26 U.S.C. 72(t) (imposing a 10 percent tax penalty on early distributions from plans). Finally, the target audience for the Trust is Retirement Plan administrators, not individual customers, thereby ensuring that the Bank and its affiliates market the Trust only as a fiduciary investment, rather than a speculative investment vehicle.

The Bank's activities as managing agent, as well as the collective investment of Retirement Plan assets themselves, would satisfy the *Camp* requirement that there be a bona fide fiduciary purpose for the combination of pooling trust assets, acting as managing agent, and purchasing stock for the account of customers to be a permissible national bank activity. As previously discussed, under the common law of trusts, a bank's activities as managing agent are fiduciary in nature. *See Scott on Trusts* 8.1, *supra*. The OCC in its regulations and interpretations similarly has stated that managing agency accounts constitute a fiduciary activity. *See* 12 C.F.R. 9.1(h); Walzer Letter, *supra*. Under banking law and ERISA, the fiduciary nature of the activity stems from the relationship between the Retirement Plans and the Bank, whereby the Bank exercises investment discretion over plan assets, with a goal of providing long-term retirement income to plan participants. *Id*.; 29 U.S.C. 1002(21)(A) (definition of "fiduciary" in ERISA includes any party exercising "any authority or control" concerning the management or disposition of plan assets).

This reasoning would extend to investment of funds held by affiliates as managing agent in the Trust, as well. *See* Horn Letter and Interpretive Letter No. 413, *both supra*. The fiduciary nature of both the Trust and the underlying managing agency activities does not change because an affiliate, as well as the Bank, might invest funds in the Trust as a managing agent. The affiliate would be subject to fiduciary duties with respect to the Retirement Plans for which it acts as managing agent -- just as the Bank itself would be with respect to the Retirement Plans for which it acted as managing agent (along with all the Retirement Plans that it invested collectively as trustee for the Trust). As noted in the Horn Letter, affiliates would also be subject to duties under the common law of trusts and ERISA when investing funds in a parent's collective fund because of the fiduciary duties created by a managing agency relationship. *See* Horn Letter, *supra*.

Nor does the Bank's proposal implicate any of the hazards that the Supreme Court found in *Camp*. There is little likelihood that plan managers or participants will lose confidence in the banking system as a result of a bank, in its role as managing agent, collectively investing Retirement Plan assets. Banks have long offered collective investment products and such activities have not undermined the confidence of plan managers or individual fiduciary customers in banks. Banks likewise long have offered managing agency accounts to customers without any discernible impact on overall confidence in the banking system. There are several prudential requirements in law that help minimize this risk. *See* 29 U.S.C. 1104(1) (diversification of investments required under ERISA); *Scott on Trusts*, *supra*, 170 and 174 (duties of care and loyalty).

As a practical matter, there is little likelihood that the Bank would lend money to the individual Retirement Plans or their participants to purchase interests in those plans, since ERISA prohibits fiduciaries from causing plans to engage in a transaction constituting a direct or indirect "lending of money or other extension of credit between the plan and a party in interest". 29 U.S.C. 1106(a)(1)(B). Since fiduciaries (including managing agents) are "parties in interest" under ERISA, this prohibition would bar the Bank, as managing agent, from lending money to a Retirement Plan to finance, for example, investments in the Trust. 29 U.S.C. 1002(14)(A). Similarly, ERISA classifies an employer whose employees participate in a plan as a "party in interest", thereby barring the Bank or its affiliates from lending money to an employer as a means of encouraging the employer to let the Bank or its affiliates act as managing agent for such a plan. *See id.* at 1002(14)(C).<**NOTE:** OCC regulations against self-dealing also would bar the Bank and its affiliates from making loans to an employer that they conditioned on the employer's agreement to designate the Bank or one of its affiliates as managing agent. *See* 12 C.F.R. 9.12.>Because contributions to Retirement Plans generally occur through payroll deductions, the Bank would not be involved in lending to Retirement Plan participants to entice them to participate in those plans.<**NOTE:** ERISA further prohibits fiduciaries from dealing "with the assets of the plan in [their] own interest or for [their] own account". 29 U.S.C. 1106(b)(1). Lending money to Retirement Plan participants to purchase interests in the Trust could be a transaction for the Bank's own interest, since these loans would increase participation in the Trust and inure to the Bank's benefit.> In addition, banks are subject to statutory and regulatory restrictions against unsafe and unsound lending activities. *See* 12 U.S.C. 92a, 161 (examination authority of the OCC), 1818(b) (cease and desist orders for unsafe or unsound practices), (e) (removal authority for banks in violation of any law or regulation, or breaches of fiduciary duty), and (i)(2) (civil money penalties for violations of law or regulation, or breaches of fiduciary duty).

The Bank also is unlikely to make unsafe loans to securities issuers in whose securities the Trust invested. Because of the diversification requirements for the Trust, the Bank would not have a strong incentive to make loans to a particular securities issuer to prop up the issuer and its securities, since one issuer's performance problems would be unlikely to have a critical impact on the value of Trust interests. Moreover, statutory and regulatory restrictions on bank lending should preclude such unsafe loans. *See generally* 12 U.S.C. 84 and 1818(b)(8); 12 C.F.R. Part 32.

A bank's decision to collectively invest fiduciary assets also is highly unlikely to create undue promotional pressures on the bank or interfere with the bank's ability to provide Trust customers disinterested investment advice, the final *Camp* hazard. We note that the Bank's target audience, plan administrators, consists of sophisticated investors who are able to evaluate the appropriateness of the Trust as an investment vehicle for their plans. Thus, there is minimal risk, if any, that the Bank would fail to give disinterested investment advice or that, if it did, such efforts would go undetected.

Conclusion

For the reasons described above, we conclude that the Bank's proposal to collectively invest Retirement Plans for which it or an affiliate acts as managing agent is a fiduciary activity permissible for national banks that does not contravene the Glass-Steagall Act. If you have any questions, please feel free to contact Lee Walzer, Senior Attorney, Securities and Corporate Practices Division, at (202) 874-5210.

Sincerely,
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