



**EMPLOYEE
OWNED 2019**

Duties and Responsibilities of Trustees
THE CONFERENCE & TRADE SHOW
for ESOPs

Duties and Responsibilities of Trustees



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#EO2019



Agenda

- ERISA Fiduciaries and ESOP Trustees
- Role of the Trustee/Key Duties
- Valuation of Employer Stock
- Allocations, Distributions, and Voting
- Purchase and Sale of Employer Stock
- Other Trustee “Stuff”
- Annual Tasks—a Checklist
- New Trustee Orientation



ERISA Fiduciary Duty Basics

- Duty of loyalty – to act solely in the interest of participants
- Exclusive Purpose rule – for the exclusive purpose of providing benefits
- Duty of prudence – prudent expert standard
- Diversification (ESOP exception – but not from prudence)
- Follow Plan documents (if not contrary to ERISA)
- Avoid conflicts of interest
- Do not engage in “prohibited transactions”



Who is a Fiduciary?

- Likely Fiduciaries:
 - Employer/Plan Sponsor
 - Board of Directors
 - Trustees
 - Members of the administrative committee
 - Officers/employees who exercise control over the investment of plan assets or plan management



Who is a Fiduciary?

- Who cannot serve as a fiduciary?
 - Persons who have committed certain crimes (robbery, bribery, extortion, murder, etc.)
- Who generally is not a fiduciary?
 - Persons who only perform ministerial functions (calculating benefits, adjudicating claims, maintaining records)
 - Third Party Administrator (TPA or Recordkeeper)
 - Valuation Firm (Company Appraiser)
 - Plan and/or Company Attorney
 - Accountants/Auditors



What does a Trustee do?

- Employer stock purchase and/or Employer stock sale transactions
 - Initial ESOP formation and Employer stock purchase
 - “Second stage” Employer stock purchase transactions
- Trustees’ Issues in connection with the day-to-day operations of an ESOP:
 - Valuation
 - Voting Employer stock/plan sponsor corporate governance issues
 - Recordkeeping and day-to-day Trust accounting
 - Recycling and repurchase issues
 - Duty to monitor fiduciaries and advisors – conflicts of interest



Trustee Role in Plan Administration

- Trustee is *not* Plan Administrator—no direct role in determining who is eligible or vested or who has what allocation under the plan (unless Trustee has also been appointed to serve as Plan Administrator).
- Trustee should verify Company is maintaining compliance with administration of plan.
- Confirm share release calculations are correct if the ESOP is leveraged



Successor Trustee Issues

- Fiduciary duty begins immediately upon assumption of fiduciary status
 - Proper documentation of resignation or removal of prior trustee and appointment of successor
 - Board resolutions, trust agreement, acknowledgement of appointment
- No fiduciary liability for breach of fiduciary duty under ERISA if the breach was committed before he/she became a fiduciary or after he/she ceased to be a fiduciary
- However, a successor trustee will be liable for failing to act if it can be proved that:
 - Successor trustee had knowledge of the breach by the predecessor (or should have known)
 - Successor trustee failed to make reasonable efforts to remedy the breach and
 - Plan's loss resulted from that failure



Read and Understand Documents that can impact the ESOP

- Always Read
 - Plan Document (Plus Amendments)
 - Plan Trust
 - By-Laws
 - Articles of Incorporation
 - Anything directly tied to stock performance
 - Stock Appreciation Rights Plan
 - Phantom Stock
 - Warrants
 - Stock Options
 - ESOP Loan Documents (if still outstanding)
 - Pledge Agreements (if still outstanding)
 - Stock Purchase or Redemption Agreement
 - All documents developed during transactions or is pertinent to the Company's performance



Read and Understand Documents that can impact the ESOP (cont.)

- Company inside:

- Company structure
- Key legal documents (Articles of Incorporation, By-Laws, etc.)
- Overall stability of the company
- Strength of client and vendor relationships
- Etc.

- Company outside:

- Know competition
- Industry
- Overall Economy and business implication



Practical Applications of the Trustee's Responsibilities

Valuation of Employer Stock

- Determining Value of Employer Stock – Trustee is responsible.
- How does the Trustee select and engage an Independent Appraiser?
- What should the Trustee do with the valuation report?
- Process for accepting the report from Independent Appraiser
- Review the report
- Ask questions
 - Review the approaches and methodologies
 - Projections and assumptions
 - Premiums and discounts
- Consider the Process Agreements



What should the Trustee do with the Valuation Report (Cont.)

- Look over the methodology
 - How many different methods were used to determine value
 - Asset Approach
 - Discounted cash flow
 - Public company comparables
 - Guideline companies methodology
 - Capitalized cash flow method
 - Merger and acquisition method

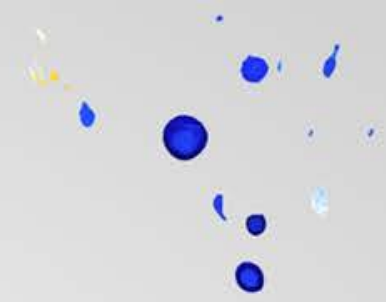


Other Valuation-related Information that the Trustee Should Consider

- Overall solvency of the Plan Sponsor
- Trends exhibited in the report
- Performance of the industry
- Plan liability versus fair market value
- Necessity of the Trustee to discuss issues with management
- Repurchase liability



Practical Applications of the Trustee's Responsibilities



Recordkeeping and Day-to-Day Trust Accounting

- Payment of an ESOP loan
 - Notify the Plan Sponsor of pending loan payments due.
 - Collect contributions from the Plan Sponsor and make necessary payments to the bank or back to the Plan Sponsor.
 - All contributions and loan payments need to be run through the trust even if the loan is from the Plan Sponsor.
 - Keep receipts!
 - Calculate the release of the shares as per the loan documents and make sure that no bank covenants have been violated.
 - Make sure to get shares released from the Pledge



Miscellaneous Recordkeeping/Trust Accounting:

- Maintain Trust checking account
- Retain and maintain custody of ESOP Stock Certificates for shares that have been released.
- Submit Annual Report and accounting to Plan Sponsor



Distributions:

- Trustee makes or oversees the distributions to participants as directed by Plan Administrator.
- Prepare the check or stock certificates (if shares are to be paid out).
 - Certificates may be prepared by legal counsel
- Compute income tax withholding. Prepare appropriate tax reporting forms and timely send withholding tax to the IRS.
 - ESOP should have its own Tax ID #



Voting of Employer Stock

- Pass-through voting normally applies under limited circumstances
 - recapitalization, reclassification, merger, consolidation, dissolution, liquidation, or sale of substantially all corporate assets
- Voting Pass-Through: Distribute “adequate” information to participants to permit an informed vote
- Participants have right to instruct Trustee on voting rights, but not to actually vote shares
- Voting Pass-Through: Confidential tabulation of participant voting directions on allocated shares and voting in accordance with those directions (Some internals have accountants compile results)
 - Does Trustee have to follow directions?
 - How does Trustee vote unallocated shares?
 - How does Trustee vote unvoted shares?
 - How does Trustee vote disqualified shares?
- Non-Pass Through Voting: Trustee votes ESOP shares on shareholder issues which are not subject to Pass-Through requirements (e.g., Election of Directors)



ESOP Stock Recycling vs. Corporate Stock Repurchase

- If the Plan Sponsor purchases distributed ESOP shares, is it a Fiduciary decision?
- If the ESOP purchases distributed ESOP shares, is it a Fiduciary decision?
- What if the Plan Sponsor offers to repurchase ESOP shares from the ESOP so that the ESOP can distribute cash in lieu of shares?
 - If Employer Stock is sold by the ESOP to the Plan Sponsor, the sale is a party-in-interest transaction and must be done at a fair market value as determined at time of the sale, not as of last annual valuation date.



Conflicts of Interest

- Officers or directors of Plan Sponsor may serve as Trustee and/or Plan Administrator
- Duty to all shareholders as officer/director, but ERISA fiduciary duty is “solely” to and for participants
- General: ESOP’s interests may conflict with management or outside shareholders
- Possible solution for conflict – Special Fiduciary



I Just Was Named A Trustee for Our New ESOP—What Do I Do?

- Open a checking account in the name of the Trust
- Make sure you have physical possession of Trust assets, including especially Employer Stock certificates not pledged as collateral on ESOP loan
- Get statements for any existing Trust accounts
- EIN for Trust
- Engage competent and qualified Independent Appraiser and ESOP counsel
- Can ESOP counsel to Plan Sponsor advise Trustee?



Which Hat is On?

- *When an executive or shareholder of the Plan Sponsor is also the Trustee, there may be a conflict (duty to stockholders v. duty to ESOP participants).*
THINK:
- *In what capacity am I acting in making this decision? Which hat do I have on and is it the correct one?*
 - Document! Document! Document!

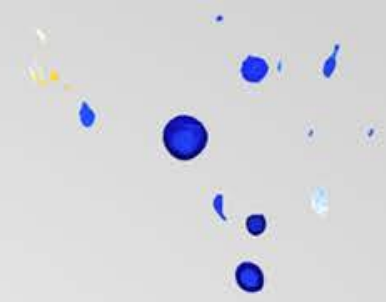


Things that Go Bump In the Night (More material under “Sticky Fiduciary Wickets”)

- DOL Audits
- Bad Internal Accounting and Record Keeping
 - Share release mistakes
 - Improper or wrong distributions
 - Failure to follow Plan terms
- Disgruntled participants
- Contests for corporate control
- Bad corporate performance
- Questionable Employer Stock valuation report and/or process



Trustee's Annual ESOP Calendar

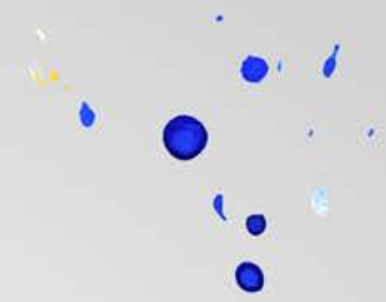


<u>Period</u>	<u>Duty</u>	<u>Description</u>
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1		Prior Quarter	Distribution	Ensure Diversification & RMD Distributions for current & next plan year
2		Prior Quarter	Investment	Engage Valuation Firm
3		Prior Quarter	Distribution	Engage Third Party Administrator
4		31-Jan *	Compliance	Last day to Prepare and Mail IRS Form 1099-R AND IRS Form 945
5		Q1	Distribution	Determine Participant Eligibility
6		28-Feb *	Compliance	Last day to Prepare and Mail IRS Form 1096
7		Q1	Investment	Review Financial Statements of underlying Company
8		15-Mar	Compliance	Last day to Receive Company Contribution for prior plan year (unless corporate return is extended)
9		Q1	Investment	Read Valuation Report & Establish Price
10		Q1	Distribution	Review Allocation Report & Distribute Participant Statements
11		Q1	Compliance	Distribute Diversification Notices
12		1-Apr *	Compliance	Last day for RMD payments to any participant who turned 70&1/2 in prior year
13		Q2	Distribution	Review & Prepare Participant Distributions
14		Q2	Corp Governance	Review Proposals & Nominated Directors
15		Q2	Corp Governance	Distribute Proxy Information to Participants
16		Q2	Compliance	Last day to Execute Diversification Elections
17		Q2	Corp Governance	Attend Annual Meeting
18		Q2	Corp Governance	Vote Proxy



Trustee's Annual ESOP Calendar



<u>Period</u>	<u>Duty</u>	<u>Description</u>
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19	Q3	Compliance	Last day to file 5500 (can be extended 2&1/2 mos.)
20	30-Sep	Compliance	Last day to Distribute Summary Annual Report (within 2 mos. after filing tax return)
21	Q4	Distribution	Review Repurchase Obligation Study
22	31-Dec *	Compliance	Last day for RMD distributions
23	Periodically	Compliance	Distribute Summary Plan Description to new participants
24	Periodically	Corp Governance	Review Corporate Actions, Budgets & Plans
25	Periodically	Corp Governance	Engage Plan & Trust Legal Advisor
26	Periodically	Custody	Collect, Receive and Invest Asset revenues (divs or S-Corp earnings)
27	Periodically	Custody	Accept Employer Contribution(s)
28	Periodically	Investment	Engage in Assets Transactions: Purchases or Sales
29	Periodically	Investment	Prepare and Process Loan Payments
30	Recurring	Compliance	Monitor Plan & Trust compliance with applicable laws & regulations
31	Recurring	Custody	Hold, Control and Maintain assets
32	Recurring	Investment	Determine Plan Investment Prudence



Merri E. Ash

Merri has over 40 years experience in Employee Benefits services. Merri's past work experience includes work as a senior trust officer with SunTrust Bank, Employee Benefits Consultant with Wyatt Company, Benefits Manager with Jonathon Corporation, an ESOP company and Team Leader and Senior Benefits Consultant with the National Automobile Dealers Association. She is a past Chairperson for the Administrative Advisory Committee of The ESOP Association, former Board of Governors member for the National ESOP Association and current Board of Trustees member for the Employee Ownership Foundation. Merri has been with TI-TRUST since 2002.

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David Whaley



David is a partner in the Employee Benefits & Executive Compensation practice group. He focuses his practice on assisting private and public companies and nonprofit organizations with all areas of employee benefits, including design, implementation and compliance in connection with tax qualified and nonqualified deferred compensation arrangements (e.g., 409A compliance), health and welfare arrangements and employee fringe benefits.

David has extensive experience in the area of employee stock ownership plans (ESOPs). His ESOP experience includes representing company sponsors of ESOPs and ESOP trustees and fiduciaries in acquisition transactions between the company, selling shareholders and the ESOP. In addition, he has worked with ESOP companies and ESOP trustees and fiduciaries in connection with acquisitions, divestitures and corporate organization once the ESOP owns company stock. Further, he assists both ESOP companies and lending institutions in connection with loans being made to ESOP companies so as to enable those companies to be able to meet their unique needs. Finally, David assists both ESOP companies and ESOP trustees and fiduciaries in connection with governmental investigations, participant claims processing, and governmental and plaintiff litigation.

In addition to his ESOP experience, David's practice encompasses assisting employers with modifying and properly administering both small and large defined benefit and defined contribution plans, supplemental retirement programs, equity compensation programs, health and welfare arrangements and employee fringe benefits programs.

In doing such, David assists nonprofit employers in drafting and administering qualified and nonqualified plans, including 403(b), 457(b) and 457(f) plans. He assists professional employer organizations (PEOs) in offering employee benefit programs to their client organizations. David also has the unique experience of assisting larger employers (both public and private) in establishing benefit programs for newly established entities resulting from corporate reorganizations. In addition, he represents plan sponsors before the Department of Labor, Internal Revenue Service and the Pension Benefit Guaranty Corporation in connection with audits of employee benefit plans.

David also helps employers comply with the mandates of the Affordable Care Act, providing counsel on the design of eligibility modifications to ensure compliance with the terms of the "pay or play" mandate in a way that both protects the employer from penalties while ensuring the continued delivery of an employee benefit that serves the employer's recruitment and retention goals.

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David Van Ness



David Van Ness is a V.P., Trust Officer for Horizon Trust & Investment Management in Carmel, Indiana. Horizon serves as Independent Trustee for a wide variety of ESOP companies across the United States. Dave is a member of the Horizon ESOP Committee, Indiana Chapter of The ESOP Association and a member of the ESOP Association's Administrative Committee. Dave has over 25 years of experience in the Employee Benefit field from compliance auditing, administration and trust work. He graduated from Indiana State University with a B.S. in Accounting and passed the CPA exam in 1989.

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