DEPARTMENT OF LABOR

Employee Benefits Security Administration

[Application No. D–11184]

Amendment to Prohibited Transaction Exemption (PTE) 75–1, Exemptions From Prohibitions Respecting Certain Classes of Transactions Involving Employee Benefit Plans and Certain Broker-Dealers, Reporting Dealers and Banks

AGENCY: Employee Benefits Security Administration.

ACTION: Final Amendment to PTE 75–1, Part II and Part V.

SUMMARY: This document amends PTE 75–1, Part II and Part V (40 FR 50845, October 31, 1975). PTE 75–1, Part II, permits the purchase or sale of a security in a principal transaction between an employee benefit plan and a broker-dealer, reporting dealer, or bank. PTE 75–1, Part V, permits an extension of credit to a plan by a broker-dealer in connection with the purchase or sale of securities. The amendment affects participants, beneficiaries and fiduciaries of employee benefit plans, and broker-dealers, reporting dealers and banks entering into the described transactions.

DATES: *Effective Date:* This amendment is effective January 1, 1975.

FOR FURTHER INFORMATION CONTACT: Brian Buyniski or Karen Lloyd, Office of Exemption Determinations, Employee Benefits Security Administration, U.S. Department of Labor, Room N–5649, 200 Constitution Avenue, NW., Washington, DC 20210, 202–693–8540. (This is not a toll free number.)

SUPPLEMENTARY INFORMATION: On April 28, 2004, notice was published in the **Federal Register** (69 FR 23216) of the pendency before the Department of Labor (the Department) of a proposed amendment to PTE 75–1, Part II and Part V. PTE 75–1 provides exemptive relief from certain of the restrictions of section 406 of the Employee Retirement Income Security Act of 1974 (ERISA or the Act), and from certain taxes imposed by section 4975(a) and (b) of the Internal Revenue Code of 1986 (the Code), by reason of section 4975(c)(1) of the Code. The amendment was proposed by the Department on its own motion, pursuant to section 408(a) of ERISA and section 4975(c)(2) of the Code, and in accordance with the procedures set forth in 29 CFR part 2570, subpart B (55 FR 32836, August 10, 1990).[1]

The notice gave interested persons an opportunity to comment or to request a hearing on the proposed amendment. The Department received three comments which are discussed below. One commenter requested a public hearing if the Department determined to modify a specific provision of the exemption. As the Department has not modified that provision in the final exemption, a public hearing will not be held with regard to this amendment.

Executive Order 12866 Statement

Under Executive Order 12866, the Department must determine whether the

[1] Section 102 of Reorganization Plan No. 4 of 1978, 5 U.S.C. App. at 214 (2000 ed.) generally transferred the authority of the Secretary of the Treasury to issue exemptions under section 4975(c)(2) of the Code to the Secretary of Labor.

In the discussion of the exemption, references to specific provisions of the Act should be read to refer as well to the corresponding provisions of section 4975 of the Code.

regulatory action is ''significant'' and therefore subject to the requirements of the Executive Order and subject to review by the Office of Management and Budget (OMB). Under section 3(f), the order defines a ''significant regulatory action'' as an action that is likely to result in a rule (1) having an annual effect on the economy of $100 million or more, or adversely and materially affecting a sector of the economy, productivity, competition, jobs, the environment, public health or safety, or State, local or tribal governments or communities (also referred to as ''economically significant''); (2) creating serious inconsistency or otherwise interfering with an action taken or planned by another agency; (3) materially altering the budgetary impacts of entitlement grants, user fees, or loan programs or the rights and obligations of recipients thereof; or (4) raising novel legal or policy issues arising out of legal mandates, the President's priorities, or the principles set forth in the Executive Order.

This amendment has been drafted and reviewed in accordance with Executive Order 12866, section 1(b), Principles of Regulation. The Department has determined that this amendment is not a ''significant regulatory action'' under Executive Order 12866, section 3(f). Accordingly, it does not require an assessment of potential costs and benefits under section 6(a)(3) of that order.

Paperwork Reduction Act

The information collection request (ICR) included in the existing PTE 75–1 is currently approved under Office of Management and Budget (OMB) control number 1210–0092 (through March 31, 2007). The amendment does not modify the information collection provisions of the exemption. Therefore, the Department has not submitted an ICR to OMB in connection with this Final Amendment to PTE 75–1.

Description of the Exemption

Part I of PTE 75–1 provides relief for agency transactions and services; [2] Part II for principal transactions; Part III for underwritings; Part IV for market-making; and Part V for extension of credit.

PTE 75–1, Part II

Part II of PTE 75–1 provides relief from the restrictions of 406(a) of ERISA and the taxes imposed by section 4975(a) and (b) of the Code, by reason of section 4975(c)(1)(A) through (D) of the Code, for the purchase or sale of a security between an employee benefit plan and: (1) A broker-dealer registered under the Securities Exchange Act of 1934 (the 1934 Act); (2) a reporting dealer who makes primary markets in securities of the U.S. Government or of any agency thereof and reports daily to the Federal Reserve Bank of New York its positions with respect to Government securities and borrowings thereon; or (3) a bank supervised by the United States or a State.[3]

The exemption further provides relief from the restrictions of section 406(b) of ERISA and the taxes imposed by section 4975(a) and (b) of the Code, by reason of section 4975(c)(1)(E) and (F) of the Code, for the purchase or sale by a plan of securities issued by an open-end investment company registered under the Investment Company Act of 1940, provided that a fiduciary with respect to the plan is not a principal underwriter for, or affiliated with, such investment company within the meaning of sections 2(a)(29) and 2(a)(3) of the Investment Company Act of 1940 (the Mutual Fund Exemption).

The conditions of PTE 75–1, Part II, require that a broker-dealer must customarily purchase and sell securities for its own account in the ordinary course of its business as a broker-dealer. The conditions further require that reporting dealers and banks must customarily purchase and sell Government securities for their own accounts in the ordinary course of their businesses, and that any purchase or sale between the plan and such reporting dealer or bank be limited to a purchase or sale of Government securities.

All transactions entered into pursuant to Part II must be at least as favorable to the plan as an arm's length transaction with an unrelated party would be, and must not be, at the time of the transaction, a prohibited transaction within the meaning of section 503(b) of the Code.

Except with respect to the Mutual Fund Exemption, Part II as originally granted provided that the broker-dealer, reporting dealer or bank may not be a fiduciary with respect to the plan, and such broker-dealer, reporting dealer or bank may be a party in interest or disqualified person with respect to the plan solely by reason of section 3(14)(B) of the Act or section 4975(e)(2)(B) of the Code or a relationship to a person described in those sections. For purposes of this condition, a broker-dealer, reporting dealer or bank is not deemed to be a fiduciary with respect to a plan solely by reason of providing securities custodial services for a plan. Lastly, the exemption for principal transactions also contains certain recordkeeping requirements.

PTE 75–1, Part V

Part V of PTE 75–1 provides relief from the restrictions of section 406 of ERISA and the related excise taxes imposed by section 4975(a) and (b) of the Code, by reason of section 4975(c)(1) of the Code, for any extension of credit to a plan by a broker or dealer registered under the 1934 Act.[4] As originally granted, Part V provided that the broker-dealer extending credit may not be a fiduciary with respect to any assets of the plan, unless no interest or other consideration is received by such fiduciary or any affiliate in connection with the extension of credit.

Under Part V, the extension of credit must be made in connection with the purchase or sale of securities, must be lawful under the 1934 Act, and may not be a prohibited transaction within the meaning of section 503(b) of the Code. Lastly, the exemption for extensions of credit also contains certain recordkeeping requirements.

Amendment

As part of the proposed amendment, the Department repositioned the following language found in section (d) of Part II of the exemption:

> Neither the restrictions of this paragraph nor (if the other conditions of this exemption are met) the restrictions of section 406(b) of the Act and the taxes imposed by section 4975(a) and (b) of the Code, by reason of section 4975(c)(1)(E) and (F) of the Code, shall apply to the purchase or sale by the plan of securities issued by an open-end investment company registered under the Investment Company Act of 1940 (15 U.S.C. 80a–1 et seq.), provided that a fiduciary with respect to the plan is not a principal underwriter for, or affiliated with, such investment company within the meaning of sections 2(a)(29) and 2(a)(3) of the Investment Company Act of 1940 (15 U.S.C. 80a–2(a)(29) and 80a–2(a)(3)).

The Department included the relief provided by this provision in a new paragraph (2) of Part II of the exemption for principal transactions. The Department also proposed to amend the language of this section to clarify that the fiduciary referenced therein is the

[2] Part I(a) expired on May 1, 1978. It ultimately was replaced by PTE 86–128 (51 FR 41686, Nov. 18, 1986).

[3] The exemption defines the terms ''broker-dealer,'' ''reporting dealer'' and ''bank'' to include such entities and any affiliate thereof. The term ''affiliate'' is defined as in 29 CFR 2510.3–21(e) and 26 CFR 54.4975–9(e).

[4] The exemption defines the terms ''broker'' and ''dealer'' to include such entities and any affiliate thereof. The term ''affiliate'' is defined as in 29 CFR 2510.3–21(e) and 26 CFR 54.4975–9(e).

fiduciary who makes the decision on behalf of the plan to enter into the transaction. The Department also requested public comment on the current utility of this exemption.

The Department additionally proposed to amend another provision of section (d) of Part II, which stated, in relevant part, that:

> Such broker-dealer, reporting dealer or bank is not a fiduciary with respect to the plan, and such broker-dealer, reporting dealer or bank is a party in interest or disqualified person with respect to the plan solely by reason of section 3(14)(B) of the Act or section 4975(e)(2)(B) of the Code or a relationship to a person described in such sections. For purposes of this paragraph, a broker-dealer, reporting dealer, or bank shall not be deemed to be a fiduciary with respect to a plan solely by reason of providing securities custodial services for a plan.

Under the proposed amendment, the exemption permits plans to engage in transactions with broker-dealers, reporting dealers, banks and their affiliates except where the broker-dealer, reporting dealer, bank or an affiliate has or exercises any discretionary authority or control (except as a directed trustee) with respect to the investment of plan assets involved in the transaction, or renders investment advice (within the meaning of 29 CFR 2510.3–21(c)) with respect to the investment of those assets.[5]

The Department likewise proposed to amend condition (a)(2) of PTE 75–1, Part V, which required that the party in interest or disqualified person providing the extension of credit to the plan:

> [i]s not a fiduciary with respect to any assets of such plan, unless no interest or other consideration is received by such fiduciary or any affiliate thereof in connection with such extension of credit.

Under the proposed amendment, section (a)(2) states that the party in interest or disqualified person extending credit to the plan:

> does not have or exercise any discretionary authority or control (except as a directed trustee) with respect to the investment of the plan assets involved in the transaction, nor does it render investment advice (within the meaning of 29 CFR section 2510.3–21(c)) with respect to those assets, unless no interest or other consideration is received by the party in interest or disqualified person or any affiliate thereof in connection with such extension of credit.

[5] Nothing herein should be construed to imply that a directed trustee is not a fiduciary under the Act. See 29 U.S.C. 103(a)(1). A plan may expressly provide that a trustee is subject to the direction of a named fiduciary who is not a trustee, in which case the trustee shall be subject to proper directions of such fiduciary which are made in accordance with the terms of the plan and which are not contrary to the Act.

Discussion of Comments

The Department received one comment concerning the effective date of the proposed amendments. The commenter requested that, with respect to the proposed amendments to condition (d) of Part II and condition (a)(2) of Part V, the Department state that it was the intention of the Department at the time of the granting of the final exemption in 1975 to focus only on fiduciaries with respect to the plan assets involved in the transaction, as opposed to any fiduciary of the plan. The commenter referenced the following language in the preamble of the proposed exemption in August 1975 regarding proposed regulations under the definition of fiduciary at section 3(21) of the Act:

> It should be noted, moreover, that under the regulations proposed in conjunction with these proposed exemptions relating to the definition of the term ''fiduciary,'' a person who is a plan fiduciary would be deemed to be a fiduciary only with respect to those plan assets with respect to which he exercises those functions which make him a fiduciary.

40 FR 33566. The Department received a follow up submission from this commenter requesting that, in order to avoid confusion and uncertainty, this amendment to PTE 75–1 be made retroactive to October 31, 1975. The Department also has been urged informally to adopt a retroactive effective date.

While the Department acknowledges that some confusion may have arisen from the fact that two conditions of PTE 75–1, Part II and Part V, regarding fiduciaries, were broader than the Department's regulations regarding the definition of a fiduciary under section 3(21) of the Act, the Department is unable to concur with the commenter that its original intent with respect to such conditions was in fact to limit them to fiduciaries with respect to the plan assets involved in the transaction.[6] The conditions contained in the Department's administrative exemptions are designed to ensure that the Department can make findings required pursuant to section 408(a) of ERISA and 4975(c)(2) of the Code that the exemption is administratively feasible, and in the interests of, and protective of the rights of, plan participants and beneficiaries. The Department's regulations do not govern the scope of the conditions of its administrative exemptions. Therefore, the fact that a regulation defining the term ''fiduciary'' may have focused on the plan assets with respect to which a person exercises fiduciary functions does not necessarily govern the meaning of a condition of an administrative exemption. Prior to this amendment, the conditions in PTE 75–1, Part II and V, clearly referred to a fiduciary with respect to a plan.

Nevertheless, in the Department's view, an interpretation of the conditions of PTE 75–1, Part II and Part V, which focused on fiduciaries with respect to the plan assets involved in the transaction would not have created an undue risk of loss of plan assets. As the Department has concluded that the amendments are sufficiently protective of plan assets on a prospective basis, the Department believes a similar conclusion would dictate in favor of granting the amendments on a retroactive basis. Accordingly, the Department has determined to make these amendments to PTE 75–1 retroactive to January 1, 1975, which is the effective date of PTE 75–1.

The Department received three comments on the current utility of the Mutual Fund Exemption. Based on the information received, the Department believes that additional time is needed to more fully consider the issues raised by the commenters. However, the Department does not wish to unduly delay finalization of the other amendments to PTE 75–1. Accordingly, this document contains final amendments to Parts II and V of PTE 75–1 and adopts the repositioning of the Mutual Fund Exemption to paragraph (2) of PTE 75–1, Part II, and adopts the clarifying language. As a result, the Mutual Fund Exemption remains in effect pending further action by the Department.

General Information

The attention of interested persons is directed to the following:

(1) The fact that a transaction is the subject of an exemption granted under section 408(a) of the Act and section 4975(c)(2) of the Code does not relieve a fiduciary or other party in interest or disqualified person with respect to a plan to which the exemption is applicable from certain other provisions of the Act and the Code, including any prohibited transaction provisions to which the exemption does not apply and the general fiduciary responsibility provisions of section 404 of the Act which, among other things, require a fiduciary to discharge his duties respecting the plan solely in the interest of the plan's participants and beneficiaries and in a prudent fashion in accordance with subsection (a)(1)(B) of section 404 of the Act; nor does it affect

[6] The Department notes that the language quoted by the commenter appeared in the preamble to Part III of PTE 75–1, which is not the subject of this amendment.

the requirement of section 401(a) of the Code that a plan must operate for the exclusive benefit of employees of the employer maintaining the plan and their beneficiaries;

(2) The Department finds that the amended exemption is administratively feasible, in the interests of the plan and of its participants and beneficiaries, and protective of the rights of participants and beneficiaries of the plan;

(3) The amended exemption is applicable to a particular transaction only if the transaction satisfies the conditions specified in the exemption; and

(4) The amended exemption is supplemental to, and not in derogation of, any other provisions of the Act and the Code, including statutory and other exemptions and transitional rules. Furthermore, the fact that a transaction is the subject of an exemption is not dispositive of whether the transaction would have been a prohibited transaction in the absence of such exemption.

Amendment

Accordingly, PTE 75–1 is amended as follows under the authority of section 408(a) of the Act and section 4975(c)(2) of the Code, and in accordance with the procedures set forth in 29 CFR part 2570, subpart B (55 FR 32836, 32847, August 10, 1990).

I. PTE 75–1, Part II, is amended in its entirety to read as follows:

(1) The restrictions of section 406(a) of the Employee Retirement Income Security Act of 1974 (the Act) and the taxes imposed by section 4975(a) and (b) of the Internal Revenue Code of 1986 (the Code), by reason of section 4975(c)(1)(A) through (D) of the Code, shall not apply to any purchase or sale of a security between an employee benefit plan and a broker-dealer registered under the Securities Exchange Act of 1934 (15 U.S.C. 78a *et seq.*), a reporting dealer who makes primary markets in securities of the United States Government or of any agency of the United States Government (''Government securities'') and reports daily to the Federal Reserve Bank of New York its positions with respect to Government securities and borrowings thereon, or a bank supervised by the United States or a State, and

(2) The restrictions of section 406(a) and 406(b) of the Act and the taxes imposed by section 4975(a) and (b) of the Code, by reason of section 4975(c)(1)(A) through (F) of the Code, shall not apply to the purchase or sale by a plan of securities issued by an open-end investment company registered under the Investment Company Act of 1940 (15 U.S.C. 80a–1 *et seq.*), provided that no fiduciary with respect to the plan who makes the decision on behalf of the plan to enter into the transaction is a principal underwriter for, or affiliated with, such investment company within the meaning of sections 2(a)(29) and 2(a)(3) of the Investment Company Act of 1940 (15 U.S.C. 80a–2(a)(29) and 80a–2(a)(3)).

The exemptions set forth in (1) and (2) above are subject to the following conditions:

(a) In the case of such broker-dealer, it customarily purchases and sells securities for its own account in the ordinary course of its business as a broker-dealer.

(b) In the case of such reporting dealer or bank, it customarily purchases and sells Government securities for its own account in the ordinary course of its business and such purchase or sale between the plan and such reporting dealer or bank is a purchase or sale of Government securities.

(c) Such transaction is at least as favorable to the plan as an arm's length transaction with an unrelated party would be, and it was not, at the time of such transaction, a prohibited transaction within the meaning of section 503(b) of the Code.

(d) Except with respect to transactions described in section (2) above, neither the broker-dealer, reporting dealer, bank, nor any affiliate thereof has or exercises any discretionary authority or control (except as a directed trustee) with respect to the investment of the plan assets involved in the transaction, or renders investment advice (within the meaning of 29 CFR 2510.3–21(c)) with respect to those assets.

(e) The plan maintains or causes to be maintained for a period of six years from the date of such transaction such records as are necessary to enable the persons described in paragraph (f) of this exemption to determine whether the conditions of this exemption have been met, except that:

(1) Such broker-dealer, reporting dealer, or bank shall not be subject to the civil penalty which may be assessed under section 502(i) of the Act, or to the taxes imposed by section 4975(a) and (b) of the Code, if such records are not maintained, or are not available for examination as required by paragraph (f) below; and

(2) A prohibited transaction will not be deemed to have occurred if, due to circumstances beyond the control of the plan fiduciaries, such records are lost or destroyed prior to the end of such six-year period.

(f) Notwithstanding anything to the contrary in subsections (a)(2) and (b) of section 504 of the Act, the records referred to in paragraph (e) are unconditionally available for examination during normal business hours by duly authorized employees of (1) the Department of Labor, (2) the Internal Revenue Service, (3) plan participants and beneficiaries, (4) any employer of plan participants and beneficiaries, and (5) any employee organization any of whose members are covered by such plan. For purposes of this exemption, the terms ''broker-dealer,'' ''reporting dealer'' and ''bank'' shall include such persons and any affiliates thereof, and the term ''affiliate'' shall be defined in the same manner as that term is defined in 29 CFR 2510.3–21(e) and 26 CFR 54.4975–9(e).

II. PTE 75–1, Part V, is amended in its entirety to read as follows:

The restrictions of section 406 of the Employee Retirement Income Security Act of 1974 (the Act) and the taxes imposed by section 4975(a) and (b) of the Internal Revenue Code of 1986 (the Code), by reason of section 4975(c)(1) of the Code, shall not apply to any extension of credit to an employee benefit plan by a party in interest or a disqualified person with respect to the plan, provided that the following conditions are met:

(a) The party in interest or disqualified person:

(1) Is a broker or dealer registered under the Securities Exchange Act of 1934; and

(2) Does not have or exercise any discretionary authority or control (except as a directed trustee) with respect to the investment of the plan assets involved in the transaction, nor does it render investment advice (within the meaning of 29 CFR 2510.3–21(c)) with respect to those assets, unless no interest or other consideration is received by the party in interest or disqualified person or any affiliate thereof in connection with such extension of credit.

(b) Such extension of credit:

(1) Is in connection with the purchase or sale of securities;

(2) Is lawful under the Securities Exchange Act of 1934 and any rules and regulations promulgated thereunder; and

(3) Is not a prohibited transaction within the meaning of section 503(b) of the Code.

(c) The plan maintains or causes to be maintained for a period of six years from the date of such transaction such records as are necessary to enable the persons described in paragraph (d) of this exemption to determine whether

the conditions of this exemption have been met, except that:

(1) If such party in interest or disqualified person is not a fiduciary with respect to any assets of the plan, such party in interest or disqualified person shall not be subject to the civil penalty which may be assessed under section 502(i) of the Act, or to the taxes imposed by section 4975(a) and (b) of the Code, if such records are not maintained, or are not available for examination as required by paragraph (d) below; and

(2) A prohibited transaction will not be deemed to have occurred if, due to circumstances beyond the control of the plan fiduciaries, such records are lost or destroyed prior to the end of such six-year period.

(d) Notwithstanding anything to the contrary in subsections (a)(2) and (b) of section 504 of the Act, the records referred to in paragraph (c) are unconditionally available for examination during normal business hours by duly authorized employees of (1) the Department of Labor, (2) the Internal Revenue Service, (3) plan participants and beneficiaries, (4) any employer of plan participants and beneficiaries, and (5) any employee organization any of whose members are covered by such plan. For purposes of this exemption, the terms ''party in interest'' and ''disqualified person'' shall include such party in interest or disqualified person and any affiliates thereof, and the term ''affiliate'' shall be defined in the same manner as that term is defined in 29 CFR 2510.3–21(e) and 26 CFR 54.4975–9(e).

Signed at Washington DC, this 30th day of January, 2006.

Ivan L. Strasfeld,

Director, Office of Exemption Determinations, Employee Benefits Security Administration, Department of Labor.

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