**U.S. Department of Labor**

Labor-Management Services Administration
Washington, D.C. 20216

Reply to the Attention of:
Barry Newman
(202) 523-8971

OPINION 81-42A
408(b)(4)

APR 6 1981

Mr. R. Philip Steinberg
Drinker, Biddle & Reath
1100 Philadelphia National Bank Building
Broad and Chestnut Streets
Philadelphia, PA 19107

Re: The Philadelphia Saving Fund Society Incentive and Investment Plan
Identification Number F-1522

Dear Mr. Steinberg:

This is in response to your letter of April 14, 1980 regarding section 408(b)(4) of the Employee Retirement Income Security Act of 1974 (ERISA). Specifically, you have requested an advisory opinion to the effect that the early redemption of certificates of deposit by the Philadelphia Saving Fund Society (PSFS) as plan sponsor and trustee for The Philadelphia Saving Fund Society Incentive and Investment Plan (the Plan) would not constitute a prohibited transaction despite the fact that the Plan was required by regulations issued by the Federal Deposit Insurance Corporation (FDIC) to pay a penalty to PSFS for the premature redemption of these time deposits.

Your letter includes the following facts and representations. The PSFS is a mutual savings bank organized under the laws of the Commonwealth of Pennsylvania with deposits insured by the FDIC. In 1968 PSFS adopted the Plan, which is a defined contribution plan, for its employees.

The Plan provides that contributions which are made to the Plan by PSFS are to be allocated to the account of each participant and, at the direction of each participant, to be distributed between investment accounts "A" and "B". Account A is a fund consisting of securities and other properties, while Account B is a fund deposited in "a savings account or other deposit" with PSFS. The amounts held in Account B have been invested in certificates of deposit issued by PSFS and in a savings account at PSFS.

By January 30, 1980 approximately $2,875,000 had been invested in certificates of deposit which had an average maturity of seven years and had an interest rate of approximately 7.75%. On that date PSFS, acting as Plan trustee, redeemed the certificates of deposit. The Plan, in accordance with FIDC regulation 12 CFR 329.4, incurred a penalty of $101,622, which was imposed on the Plan by PSFS in its capacity as the issuer of the certificates. Of the remaining funds half were invested in a 231 day certificate at an interest rate of 13.98% and half were invested in 30 day certificates which paid between 13.4% and 17.25% annual interest.

It was intended that these funds would eventually be invested in a 2 1/2 year certificate of deposit which would pay a rate of not less than 12% per annum. PSFS has determined that by reason of the reinvestment of the Plan's assets the penalties imposed on the Plan would have been recovered by September 24, 1980, at the latest. Subsequent to that date the earnings of Account B will reflect the greater interest rates now available.

Section 404(a) provides, in part, that a fiduciary shall perform his duties with care, skill and prudence and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of like character and with like aims. Thus, a plan fiduciary has, under section 404, an affirmative duty to act in the interests of the plan and its participants and beneficiaries and cannot remain inactive when it is clearly not prudent to do so.

Section 406(a)(1) of ERISA, in part, prohibits a fiduciary with respect to a plan from causing the plan to engage in a transaction if he or she knows or should know that such a transaction constitutes a direct or indirect sale or exchange of any property between the plan and a party in interest, or the transfer to, or use by or for the benefit of, a party in interest, of any assets of the plan. In addition sections 406(b)(1) & (2) of ERISA provide, in part, that a fiduciary with respect to a plan shall not deal with the assets of the plan in his or her own interest or for his or her account or in his or her individual or in 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 interests of the plan or the interests of its participants or beneficiaries.

However, as you have noted in your letter, section 408(b)(4) of ERISA provides that the prohibitions provided in section 406 shall not apply to the investment of all or part of a plan's assets in a bank or similar financial institution supervised by the United States or a state, if such bank or other institution is a fiduciary and if the plan covers only employees of such bank or other institution. The term "deposits" as used in section 408(b)(4) is defined in the Department of Labor regulation section 2550.408b-4 to include certificates of deposit issued by the bank. This regulation also provides that the exemption contained in section 408(b)(4) shall encompass the prohibited transaction provisions of section 406(a)(1) and those of sections 406(b)(1) and (2) but shall not exempt the fiduciary from the fiduciary duties of section 404(a) of ERISA or from transactions described in section 406(b)(3), relating to the receipt of any consideration by a fiduciary from any party dealing with the plan in connection with a transaction involving the assets of the plan.

The Department of Labor has adopted an advisory opinion procedure (ERISA Procedure 76-1), which describes the general procedures for issuing information letters and advisory opinions under ERISA. In section 5 of this Procedure the Department states that it ordinarily will not issue advisory opinions relating to section 404(a) of ERISA.

In addition the Department will generally not issue an advisory opinion with respect to a completed transaction. However, because this is a situation that is likely to arise many times in the future, we have decided this matter is the appropriate subject of an advisory opinion with respect to the section 406 issues.

Since section 408(b)(4) is limited, among other restrictions, to deposits in a bank or similar financial institution supervised by the United States or a State, it is clear that Congress intended that deposits for which the exemption contained in that section is available would be subject to federal or state banking regulation. In §2550.408b-4(c)(3), moreover, the Department has recognized that the term "deposits" includes certificates of deposit which, like those at issue in this matter, are other than temporary deposits and which, therefore, may be subject to penalties upon premature redemption under federal or state banking regulation. Under these circumstances, we think that the statutory exemption encompasses the payment by a plan to a bank or similar financial institution of penalties required under federal or state banking regulation upon premature redemption. Accordingly, the payment by the Plan to PSFS of the penalty in question would, in our view, be subject to the exemption set forth in section 408(b)(4), to the extent that the exemption was available with respect to the certificates of deposit.

The exemption in section 408(b)(4), however, does not affect the applicability of the fiduciary duties set forth in section 404(a) of ERISA, in particular, the prudence rule set forth in section 404(a)(1)(B). See Conference Report accompanying ERISA (H. Rep. No. 93-1280; 93rd Cong. 2d Sess.) at page 313. We express no opinion on the question whether the redemption of the certificates of deposit by PSFS in its capacity of plan trustee was consistent with section 404(a).

This letter constitutes an advisory opinion under ERISA Procedure 76-1. Accordingly, this letter is issued subject to the provisions of the procedure, including section 10 thereof, relating to the effect of advisory opinions.

Sincerely,

Alan D. Lebowitz
Assistant Administrator for Fiduciary Standards
Pension and Welfare Benefit Programs