

U.S. Department of Labor

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



Reply to the Attention of:

OPINION NO. 82-65A
Sec. IRC §4975(c)(1), IRC §4975(e)(3)

DEC 14 1982

Mr. Homer L. Elliot
Attorney for the Philadelphia Saving Fund Society
Drinker, Biddle & Reath
Broad and Chestnut Streets
Philadelphia, Pennsylvania 19107

Re: Identification Number F-2258

Dear Mr. Elliot:

This is in response to your request for an advisory opinion from the Department of Labor concerning the application of the prohibited transaction provisions of section 4975 of the Internal Revenue Code (the Code)¹ to payments by the Philadelphia Saving Fund Society (PSFS) to certain investment brokerage firms in connection with the establishment of individual retirement accounts (IRAs) at PSFS.

Your letter contains the following facts and representations.

PSFS is a mutual savings bank which, as one of its services to its depositors, sponsors IRAs for use by its depositors. Occasionally, individuals are referred to PSFS by certain investment brokerage firms who become aware that the individuals are interested in establishing IRAs. If an IRA is subsequently established by the individual at PSFS, the funds contributed to it (or transferred to it) are invested in PSFS's time deposits. To encourage referrals, PSFS wishes to pay "finder's fees" to the referring investment brokerage firms when the referred individuals actually establish IRAs at PSFS.

¹ Although IRAs generally are not covered under Title I of the Employee Retirement Income Security Act of 1974 (ERISA), certain IRAs may be considered to be established or maintained by an employer and would thus be covered by Title I of ERISA. See Department of Labor Regulations section 2510.3-2(d). Any reference to section 4975 of the Code in this letter may be considered to refer to corresponding sections of Title I of ERISA when applicable to Title I IRA.

You present the following situations in which the finder's fee would be paid:

1. When the individual referred to PSFS has no other IRAs;
2. When the individual referred to PSFS has established one or more IRAs at other financial institutions in previous years;
3. When the individual referred to PSFS has established an IRA at another institution in the same taxable year as the PSFS IRA's establishment;
4. When the individual referred to PSFS has previously established a PSFS IRA. In this case the finder's fee would be paid with respect to the establishment of an additional IRA;
5. When the individual referred to PSFS rolls over or transfers funds from another IRA to a newly established PSFS IRA.

In all of the above situations you represent that the finder's fee would be paid before the establishment of the PSFS IRA in question, and that if no IRA were established at PSFS, the fee would be returned to PSFS by the investment brokerage firm. The amount of the fee would be approximately \$20 to \$40 for contributions of \$1,000 to \$2,000. For contributions above \$2,000 the amount of the fee would be approximately two percent of the intended contribution.

You have asked for advisory opinions to the effect that:

1(a) The payment by PSFS of a finder's fee to an investment brokerage firm which refers an individual to PSFS for the establishment of a PSFS IRA would not be a prohibited transaction under section 4975(c)(1) of the Code (or section 406 of ERISA), provided the fee is paid before the establishment of the PSFS IRA and provided there is no other IRA in existence prior to the establishment of the PSFS IRA.

(b) The payment by PSFS of a finder's fee to an investment brokerage firm which refers an individual to PSFS for the establishment of a PSFS IRA would not be a prohibited transaction under section 4975(c)(1) of the Code (or section 406 of ERISA), even if the individual owned one or more IRAs to which he or she contributed out of his or her personal service income with respect to an earlier taxable year or to which he or she rolled over a distribution from a qualified plan, provided the fee is paid before the establishment of the PSFS IRA.

(c) The payment by PSFS of a finder's fee to an investment brokerage firm which refers an individual to PSFS for the establishment of a PSFS IRA would not be a prohibited transaction under section 4975(c)(1) of the Code (or section 406 of ERISA), even if the individual had already established (or established in the future) an IRA at another institution to which he or she makes contributions for the same taxable year as the year

for which he or she contributes to the PSFS IRA, provided the fee is paid before the establishment of the PSFS IRA.

2. The payment by PSFS of a finder's fee to an investment brokerage firm which refers an individual to PSFS for the establishment of a PSFS IRA would not be a prohibited transaction under section 4975(c)(1) of the Code (or under section 406 of ERISA) even if the finder's fee is paid when a future contribution is made by the individual to another, newly-established PSFS IRA, provided the fee is paid before the establishment of the future PSFS IRA.

3. The payment by PSFS of a finder's fee to an investment brokerage firm which refers an individual to PSFS for the establishment of a PSFS IRA would not be a prohibited transaction under section 4975(c)(1) of the Code (or under section 406 of ERISA) even if the individual transfers or rolls over funds already in an IRA to the newly-established PSFS IRA, provided that the investment brokerage firm is neither a disqualified person nor a fiduciary with respect to the IRA.

Section 4975 of the Code imposes a tax on prohibited transactions. Among the transactions prohibited is a direct or indirect act by a disqualified person who is a fiduciary whereby he or she deals with the income or assets of a plan in his or her own interest or for his or her own account (section 4975(c)(1)(E) of the Code) or the direct or indirect receipt of any consideration for his or her own personal account by any disqualified person who is a fiduciary from any party dealing with the plan in connection with a transaction involving the income or assets of the plan (section 4975(c)(1)(F) of the Code).

Section 4975(e)(2)(A) of the Code defines the term disqualified person with respect to a plan to include a fiduciary.

Section 4975(e)(3) of the Code defines the term fiduciary:

(3) FIDUCIARY -- For purposes of this section, the term "fiduciary" means any person who --

(A) exercises any discretionary authority or discretionary control respecting management of such plan or exercises any authority or control respecting management or disposition of its assets,

(B) renders investment advice for a fee or other compensation, direct or indirect, with respect to any moneys or other property of such plan, or has any authority or responsibility to do so, or

(C) has any discretionary authority or discretionary responsibility in the administration of such plan.

Department of Treasury Regulations section 54.4975-9(c) provides

(c) INVESTMENT ADVICE (1) A person shall be deemed to be rendering "investment advice" to an employee benefit plan, within the meaning of section 4975(e)(3)(B) and this paragraph, only if:

(i) Such person renders advice to the plan as to the value of securities or other property, or makes recommendations as to the advisability of investing in, purchasing, or selling securities or other property; and

(ii) Such person either directly or indirectly (e.g., through or together with any affiliate) --

(A) has discretionary authority or control, whether or not pursuant to agreement, arrangement or understanding, with respect to purchasing or selling securities or other property for the plan; or

(B) Renders any advice described in paragraph (c)(1)(i) of this section on a regular basis to the plan pursuant to a mutual agreement, arrangement or understanding, written or otherwise, between such person and the plan or a fiduciary with respect to the plan, that such services will serve as a primary basis for investment decisions with respect to plan assets, and that such person will render individualized investment advice to the plan based on the particular needs of the plan regarding such matters as, among other things, investment policies or strategy, overall portfolio composition, or diversification of plan investments.

Although the payment of the finder's fee by PSFS to the referring investment brokerage firm will be made before the establishment of an IRA, receipt of the finder's fee becomes unconditional only after the IRA is established. Accordingly, for purposes of interpreting section 4975 of the Code, the transaction involving the payment of finder's fees becomes unconditional essentially at the moment that the IRA comes into existence, and it is at that point that a determination is made whether the transaction is prohibited.

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

Whether an investment broker has become a fiduciary to the PSFS IRA is a factual matter that is peculiar to each individual transaction. The Department will not ordinarily issue advisory opinions where the nature of the problem is inherently factual. See section 5.01 of ERISA Procedure 76-1 (41 FR 36281, August 27, 1976). We are unwilling, therefore, to give you an advisory opinion with respect to the issues set forth in paragraphs 1(a), 1(b), 1(c) and 2 of your request. We are happy to provide you, however, with the following general information.

If an investment broker is a fiduciary within the meaning of section 4975(e)(3) of the Code, the receipt of the finder's fee would be a prohibited transaction described in section 4975(c)(1)(F) of the Code. The investment broker may also have engaged in the prohibited transaction described in section 4975(c)(1)(E) of the Code. With respect to whether the investment broker is a fiduciary with respect to an IRA, one should consider carefully the language of Department of the Treasury Regulations section 54.4975-9(c)(1)(ii)(B), in addition to the general language of section 4975(e)(3)(A) and 4975(e)(3)(C) of the Code.

With respect to the issue set forth in paragraph 3 of your request, you have added the proviso that the investment broker is neither a disqualified person nor a fiduciary with respect to the previously established IRA. It is not clear from your submission whether, in framing the issue set forth in paragraph 3, you considered the previously established IRA as a different plan from the PSFS IRA. For purposes of this letter, we assume you meant that the investment broker is neither a disqualified person nor a fiduciary with respect to the IRA either before or after the rollover. However, we note that the referral to PSFS by the investment broker may constitute the rendering of investment advice within the meaning of section 4975(e)(3)(B) of the Code so as to make the investment broker a fiduciary. Assuming that our understanding of the proviso is correct, it is not clear to us, on the basis of the information you have supplied, what aspect of the proposed transactions you believe might be prohibited. For example, an arrangement pursuant to which PSFS IRAs pay a "service" fee to PSFS that includes reimbursement for promotional expenses -- such as the finder's fees referred to in your letter -- would present the issue whether the service arrangement qualifies for the statutory exemption contained in section 4975(d)(2) of the Code. However, we will not express an opinion with respect to paragraph 3 of your request because you have not described the facts and issues in sufficient detail. See sections 6.02(b) and (c) of ERISA Proc. 76-1.

Sincerely,

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