U.S. Department of Labor Pension and Welfare Benefits Administration
Washington, D.C. 20210

APR 5 1988

88-08A
Sec. 408(b)(3)

Mr. Thomas R. Hoecker
Snell and Wilmer
3100 Valley Bank Center
Phoenix, AZ 85073

Re: Identification No. F-3259A

Dear Mr. Hoecker:

This is in response to your letter of January 10, 1986 and subsequent correspondence requesting an advisory opinion regarding the application of Department of Labor regulation 29 CFR 2550.408b-3(h).

You represent that the Investment Incentive Plan for Employees of the Valley National Bank of Arizona (the Plan) was converted, effective January 1, 1986, into a stock bonus plan with an employee stock ownership plan (ESOP) constituting a portion of the Plan. The ESOP portion of the Plan allows the Plan's fiduciaries to borrow funds from parties in interest or others in order to finance the purchase of employer securities. Any employer securities acquired with the proceeds of such a loan will be allocated to a loan suspense account established pursuant to applicable plan provisions. It is anticipated that employer securities generally will be released from the loan suspense account and will be allocated to the participants' ESOP accounts on a monthly basis as the loan is repaid. You further represent that the loan agreement will specifically indicate whether securities will be released from the loan suspense account on a monthly or annual basis, and that the released securities will be allocated to the participants' accounts on the same basis. You represent that, if the securities are released on a monthly basis, the aggregate number of securities released from encumbrance during the plan year would equal or exceed the number of securities which must be released on an annual basis pursuant to the formula set forth in 29 CFR 2550.408b-3(h).

In effect, you request an opinion that the release of employer securities from the suspense account on an annual or a monthly basis complies with the requirements of 29 CFR 2550.408b-3(h).

Regulation section 2550.408b-3(h) specifies the basis upon which securities used as collateral in connection with an "exempt loan" under section 408(b)(3) of the Employee Retirement Income

Security Act of 1974 (ERISA) must be released from a suspense account. The general rule is that:

> (h) Release from encumbrance -- (1) General rule. In general, an exempt loan must provide for the release from encumbrance of plan assets used as collateral for the loan under this paragraph. For each plan year during the duration of the loan, the number of securities released must equal the number of encumbered securities held immediately before release for the current plan year multiplied by a fraction. The numerator of the fraction is the amount of principal and interest paid for the year. The denominator of the fraction is the sum of the numerator plus the principal and interest to be paid for all future years. See §2550.408b-3(h)(4). The number of future years under the loan must be definitely ascertainable and must be determined without taking into account any possible extensions or renewal periods. If the interest rate under the loan is variable, the interest to be paid in future years must be computed by using the interest rate applicable as of the end of the plan year. If collateral includes more than one class of securities, the number of securities of each class to be released for a plan year must be determined by applying the same fraction to each class.

An alternate rule is provided where the number of securities to be released is determined solely with regard to principal payments. It provides that:

> (2) Special rule. A loan will not fail to be exempt merely because the number of securities to be released from encumbrance is determined solely with reference to principal payments. However, if release is determined with reference to principal payments only, the following three additional rules apply. The first rule is that the loan must provide for annual payments of principal and interest at a cumulative rate that is not less rapid at any time than level annual payments of such amounts for 10 years. The second rule is that interest included in any payment is disregarded only to the extent that it would be determined to be interest under standard loan amortization tables. The third rule is that subdivision (2) is not applicable from the time that, by reason of a renewal, extension, or refinancing, the sum of the expired duration of the exempt loan, the renewal period, the extension period, and the duration of a new exempt loan exceeds 10 years.

While the number of securities that must be annually released from encumbrance is specified in the regulation, the timing of the release of such securities within the plan year is not specifically addressed. In the Department's view, the regulation does not preclude the release of securities on a monthly basis insofar as the aggregate number of securities released from encumbrance during each plan year at least equals the number of securities which must be released on an annual basis pursuant to 29 CFR 2550.408b-3(h).

In evaluating the propriety of releasing employer securities from the suspense account on a monthly or annual basis, plan fiduciaries must also consider the general fiduciary responsibility provisions of sections 403(c)(1) and 404 of ERISA. Section 403(c)(1) provides, in part, that the assets of a plan be held for the exclusive purpose of providing benefits to participants in the plan and their beneficiaries. Similarly, section 404(a)(1) of ERISA requires, in part, that fiduciaries discharge their duties with respect to a plan solely in the interest of the participants and beneficiaries of the plan, and for the exclusive purpose of providing benefits to participants and their beneficiaries.

We further note that section 404(a)(1) (D) of ERISA provides that fiduciaries must discharge their duties in accordance with the documents and instruments governing the plan insofar as they are consistent with the provisions of Titles I and IV of ERISA.

This letter is an advisory opinion under ERISA Procedure 76-1. Section 10 of the procedure explains the effect of an advisory opinion. This letter relates only to the issue that you have specifically raised in your request. Specifically, you have not asked for, and we have not expressed, any opinion with respect to whether the arrangement you propose actually provides for the release during each plan year of the number of securities required by 29 CFR 2550.408b-3(h), or whether it complies with the other requirements of 2550.408b-3 and the general fiduciary responsibility provisions of ERISA, or is in accordance with the documents and instruments governing the Plan.

Sincerely,

Robert J. Doyle
Acting Associate Director for Regulations and Interpretations