

U.S. Department of Labor

Pension and Welfare Benefits Administration
Washington, D.C. 20210



88-09A

Sec. IRC 4975(c)(1)(A), (D) & (E)

Mr. Lloyd V. Crawford
Rushton, Stakely, Johnston & Garrett
184 Commerce Street
Montgomery, AL 36104

Re: Bank of Prattville
Identification Number: F-3677A

Dear Mr. Crawford:

This is in response to your letters of May 29 and June 18, 1987 requesting an advisory opinion regarding the application of the prohibited transaction provisions of section 4975 of the Internal Revenue Code of 1986 (the Code). In particular, your letter concerns purchases of stock of the parent (the Parent) of the Bank of Prattville (the Bank) by various self-directed individual retirement accounts (IRAs) sponsored by the Bank.

You represent that the Bank is a banking corporation organized under the laws of the state of Alabama and is wholly-owned by the Parent. The Bank qualifies under section 408(a)(2) and 408(n) of the Code as a trustee of IRAs.

The Bank is considering amending the existing master and prototype IRA for which it serves as custodian to include a self-directed feature which permits the participants to direct the investments of their accounts in securities selected by the participants, including stock of the Parent. Pursuant to these amendments, the participants will have complete and sole discretion over the investments, with the Bank acting only as a non-discretionary trustee or custodian. The Bank will not make any investments or dispose of any investments for the IRAs except upon the written direction of the participants. Neither the Bank nor the Parent will provide any form of investment advice or make investment recommendations. Purchases and sales of securities will be conducted through brokerage accounts which the IRA participants will establish with the Bank.

Parent stock is not traded on any exchange or on the national over-the-counter market system. In cases where an IRA participant directs that funds in his or her account be invested in Parent stock, the stock would be purchased either from the Parent's treasury or from unrelated third parties.

You ask for an opinion with respect to the following questions:

(1) Will purchases of Parent stock by the Bank as custodian of its IRAs on behalf of and at the sole direction of participants who are neither executive officers nor directors of the Bank constitute prohibited transactions within the meaning of Code section 4975(c)(1), when the purchase is made directly from the Parent's treasury?

(2) Will purchases of Parent stock by the Bank as custodian of its IRAs on behalf of and at the sole direction of participants who are executive officers or directors of the Bank constitute prohibited transactions within the meaning of Code section 4975(c)(1), when the purchase is made directly from the Parent's treasury?

(3) Will purchases of Parent stock by the Bank as custodian of its IRAs on behalf of and at the sole direction of participants who are neither executive officers nor directors of the Bank constitute prohibited transactions within the meaning of Code section 4975(c)(1), when the purchase is made directly from a third party who is neither an executive officer or director of the Bank?

(4) Will purchases of Parent stock by the Bank as custodian of its IRAs on behalf of and at the sole direction of participants who are executive officers or directors of the Bank constitute prohibited transactions within the meaning of Code section 4975(c)(1), when the purchase is made directly from a third party who is neither an executive officer or director of the Bank?

(5) Will purchases of Parent stock by IRA custodians other than the Bank on behalf of and at the sole direction of participants who are executive officers or directors of the Bank constitute prohibited transactions within the meaning of Code section 4975(c)(1), whether the purchase is made directly from a third party or from the Parent's treasury?

Pursuant to section 2510.3-2(d) of the Department's regulations, the Department does not have jurisdiction under Title I of the Employee Retirement Income Security Act (ERISA) over those individual retirement accounts described in section 408(a) of the Code which comply with the provisions of that section of the regulation.¹ Such IRAs are within the purview of Title II of

¹ Under the regulation, Title I is inapplicable only if: (1) no contributions to the plan are made by the employer or employee association; (2) participation is completely voluntary for employees or members; (3) the sole involvement of the employer or employee organization is to permit the sponsor to publicize the program and to collect contributions on behalf of the sponsor through payroll deductions or dues checkoffs; and (4) the employer or employee organization receives no consideration in the form of cash or otherwise, other than reasonable compensation for services actually rendered in connection with payroll deductions or dues checkoffs.

ERISA, section 4975 of the Code. Under Presidential Reorganization No. 4 of 1978, effective December 31, 1978, the authority of the Secretary of the Treasury to issue interpretations regarding section 4975 of the Code has been transferred, with certain exceptions not here relevant, to the Secretary of Labor and the Secretary of the Treasury is bound by the interpretations of the Secretary of Labor pursuant to such authority. To the extent there is Title I jurisdiction regarding any IRA for which the Bank serves as custodian or trustee, references to specific sections of the Code in this letter shall also refer to the corresponding sections of ERISA.

Section 4975(c)(1) of the Code prohibits, in relevant part, the sale or exchange of property between a plan and a disqualified person (4975(c)(1)(A)), the furnishing of goods or services between a plan and a disqualified person (4975(c)(1)(C)), the use by or for the benefit of a disqualified person of the income or assets of a plan (4975(c)(1)(D)) and an 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 (4975(c)(1)(E)).

Section 4975(e)(2) of the Code defines the term “disqualified person” to include a plan fiduciary and a person providing services to a plan.

Thus, the Bank is a disqualified person with respect to the IRAs. The Parent, however, is not a disqualified person with respect to the IRAs solely by reason of its ownership of the Bank.² The question of whether the Parent is a disqualified person with respect to the IRAs under any other provision of section 4975(e)(2) of the Code is inherently factual in nature. Section 5.01 of Advisory Opinion Procedure 76-1 (ERISA Proc. 76-1, 41 FR 36281, August 27, 1976) states that the Department generally will not issue opinions on such questions.

Therefore, with respect to questions 1 and 2, to the extent that the Parent is not a disqualified person with respect to the IRAs, purchases of stock from the Parent by the Bank on behalf of and at the direction of the IRA participants would not involve transactions described in section 4975(c)(1)(A) of the Code.

With respect to questions 3 and 4, it is the Department’s opinion that if the seller of the Parent stock is not otherwise a disqualified person with respect to an IRA, the purchase by the Bank of Parent stock from unrelated third parties on behalf of the IRA does not constitute a transaction described in section 4975(c)(1)(A) of the Code.

² However, the Department notes that the Parent may be a party in interest with respect to any IRAs sponsored by the Bank which are within the jurisdiction of Title I of ERISA. In this regard, contrast section 3(14)(H) of ERISA with section 4975(e)(2)(H) of the Code.

With respect to question 5, regarding purchases of Parent stock by IRA custodians other than the Bank on behalf of and at the sole direction of participants who are officers or directors of the Bank from the Parent or an unrelated third party, it is our view that the purchases of Parent stock do not constitute transactions described in section 4975(c)(1)(A) of the Code to the extent that the seller of Parent stock is not disqualified person with respect to the IRA.³

However, while the Parent may not be a disqualified person with respect to the IRAs sponsored by the Bank, purchases and holding of Parent stock by the self-directed IRAs of officers and directors of the Bank raise questions under section 4975(c)(1)(D) and (E) of the Code, depending on the degree (if any) of the participant's interest in the transaction. The IRA participants, as officers and directors of the Bank, may have interests in the proposed transactions which may affect their best judgment as fiduciaries of their IRAs. In such circumstances, the transactions may violate section 4975(c)(1)(D) and (E) of the Code.

In addition, although the Bank may have no discretion in selecting the investments to be made by the IRAs, it appears that the Bank may have discretion in determining the seller from which the IRAs will purchase Parent stock. To the extent that it does have such discretion, the Bank would be a plan fiduciary with respect to its exercise of such discretion.

Thus, if the IRA participants do not instruct the Bank with respect to such matters, but, rather, rely on it as a fiduciary to select appropriate sellers for the transactions, a selection by the Bank of the Parent as seller would raise questions under section 4975(c)(1)(D) and (E) of the Code. This is because the Bank, as a wholly-owned subsidiary of the Parent, has an interest in the fortunes of the Parent. Therefore, the Bank may be in a position to indirectly use the assets of a plan for its own benefit or to deal with the assets of a plan in its own interest.⁴

We note that you have not requested and consequently the Department is not offering an opinion regarding the provision of brokerage services by the Bank to the IRAs.

This letter constitutes an advisory opinion under ERISA Procedure 76-1. Section 10 of the procedure describes the effect of advisory opinions.

³ We are assuming for the purposes of this letter that the Bank is not acting as an employer, as defined in section 4975(e)(2)(C) of the Code and section 3(14)(C) of ERISA, with respect to the IRAs of officers and directors of the Bank. See Advisory Opinion 85-26, April 10, 1985.

⁴ We assume, for purposes of this ruling, that the Bank does not have any authority or responsibility to vote or otherwise deal with Parent stock held by its self-directed IRAs.

Sincerely,

Robert J. Doyle
Acting Associate Director for Regulations and interpretations