

Prohibited Transaction Exemptions

A Practical Guidance® Practice Note by

José M. Jara, Fox Rothschild LLP (adapted from Lexis Tax Advisor, Edward Zelinsky)

(updated by Edward Thomas Veal, Steptoe & Johnson LLP)



José M. Jara
Fox Rothschild LLP

This practice note addresses exemptions to the prohibited transactions rules of the Employee Retirement Income Security Act of 1974 (ERISA) and the similar rules under the Internal Revenue Code. Practitioners, plan service providers, and plan fiduciaries (and other parties in interest / disqualified persons) can use this practice note in identifying exemptions to prohibited transactions. For a definition of those terms, see “Parties in Interest and Disqualified Persons” in [Prohibited Transactions](#).

The specific topics addressed in this practice note are:

- Statutory Exemptions
- Individual Exemptions
- Application for Class Exemptions
- EXPRO (Expedited Processing) Applications for Exemption

For related content, see [Prohibited Transactions](#), [Prohibited Transaction and Parties in Interest Checklist \(ERISA Rules\)](#), and [Prohibited Transaction and Disqualified Persons Checklist \(IRC Rules\)](#). Also see [ERISA Fiduciary Duties – Prohibited Transaction Rules](#).

Statutory Exemptions

ERISA identifies 23 exemptions from ERISA Section 406 and an equal number are exempted from I.R.C. Section 4975. ERISA §§ 406, 408(b), (c), and (e) (29 U.S.C.

§§ 1106, 1108(b), (c), and (e)); I.R.C. § 4975(d). Some of these exemptions are narrow in scope. Still others are so narrow as to be useless without supplementary administrative exemptions (like the prohibition on loans, including participant loans). Unless otherwise specified, in any discussion of exemptions from transactions that are prohibited by both ERISA and the IRC, “party in interest” refers to both parties in interest and disqualified persons.

The prohibited transaction exemptions protect transactions from sanctions under ERISA §406 or I.R.C. Section 4975, but they do not offer any relief from ERISA’s fiduciary standards. A transaction that meets all of the conditions for an exemption may nonetheless breach the fiduciary duties set forth in ERISA §404.

Moreover, the Department of Labor (DOL) has consistently taken the position that exemptions are available to only a very limited extent for transactions that are prohibited by ERISA §406(b), viz., dealing with plan assets for the fiduciary’s own benefit, acting on behalf of parties with interests adverse to the plan, or receiving personal consideration from parties dealing with the plan. If, for example, a fiduciary approves a loan to a participant on the understanding that the loan proceeds will be used for the fiduciary’s benefit, two transactions are deemed to have taken place: a plan loan and the receipt of personal consideration by the fiduciary. An exemption is available for the former, but not for the latter. 29 C.F.R. §2550.408b-1(a)(2).

Similarly, if a fiduciary selects himself or herself or a person in which he or she has a particular interest (e.g., a relative or a company that he or she works for) as a service provider, one transaction—the provision of services to the plan—is eligible for the exemption, but not the other (i.e.,

dealing with plan assets for the fiduciary's own benefit). 29 C.F.R. § 2550.408b-2(e); Treas. Reg. § 54.4975-6(a)(5).

Limitations on Exemptions for “Owner-Employees”

Most statutory exemptions are not available to a limited group of parties in interest, identified as “owner-employees.” This disfavored class consists of:

- Partners who have more than a 10% capital or profits interest in a plan sponsor that is organized as a partnership (or a limited liability company taxed as a partnership)
- Sole proprietors of unincorporated plan sponsors
- Officers or employees of S corporations who own more than 5% of the corporation's stock
- Owners of individual retirement accounts or annuities – and–
- Employers or associations of employers that establish IRA programs for their employees

ERISA § 408(d)(1), (d)(2)(A)(i), (ii), and (iii) (29 U.S.C. § 1108(d)(1), (d)(2)(A)(i), (ii), and (iii)); I.R.C. §§ 401(c)(3)(A), (B), 4975(f)(6)(B), (i), (ii), (iii), (C). Shareholders of C corporations or of LLCs that are taxed as corporations are not owner-employees, regardless of their ownership percentage.

The general rule is that prohibited transactions exemptions are not available to owner-employees for any transaction in which a plan lends money, pays compensation for personal services, or buys property from or sells it to an owner-employee or a party in interest closely related to an owner-employee. Related parties consist of family members (spouse, ancestors, lineal descendants, and siblings). See I.R.C. § 267(c)(4). Corporations in which the owner-employee has a 50% or greater ownership interest (measured by either voting power or share value). ERISA § 408(d)(1) (29 U.S.C. § 1108(d)(1)); I.R.C. § 4975(f)(6)(A). Two exceptions apply to this owner-employee limitation:

- Owner-employees may receive a plan loan under I.R.C. Section 72(p) rules (but an IRA owner cannot receive an IRA loan without it being treated as a distribution).
- S corporation shareholders or their related parties can sell employer stock to an employee stock ownership plan.

ERISA § 408(d)(2)(B), (C) (29 U.S.C. § 1108(d)(2)(B), (C)); I.R.C. § 408(e)(8).

Furnishing of Services or Office Space

A commonly used and important prohibited transaction exemption permits plans to make reasonable arrangements

with a party in interest for office space, or legal, accounting, or other services necessary for the establishment or operation of the plan. No more than reasonable compensation can be paid for such office space or services. ERISA § 408(b)(2) (29 U.S.C. § 1108(b)(2)); I.R.C. § 4975(d)(2).

The “reasonable compensation” exemption is critical as service providers to a plan are, by definition, parties in interest, and would otherwise be prohibited from providing services to an ERISA plan, at all. See ERISA § 3(14)(B) (29 U.S.C. § 1002(14)(B)). A service is “necessary” if it “is appropriate and helpful to the plan obtaining that service in carrying out the purposes for which the plan is established or maintained.” 29 C.F.R. § 2550.408b-2(b); Treas. Reg. § 54.4975-6(a)(2). The question then is “What is reasonable compensation?”

A related exemption permits plan fiduciaries to receive reasonable compensation for their services to the plan, with the caveat that full-time employees of the employer maintaining the plan, an employer association whose members contribute to the plan, or a union whose members are covered by the plan may receive only expense reimbursements. See ERISA § 408(c)(2) (29 U.S.C. § 1108(c)(2)); I.R.C. § 4975(d)(10). Fiduciaries may also serve as employees, agents, or representatives of parties in interest without a per se violation of the prohibition against acting for parties with interests adverse to the interests of the plan. See ERISA § 408(c)(3) (29 U.S.C. § 1108(c)(3)); I.R.C. § 4975(d)(11).

Reasonable Compensation

Compensation that would not be an ordinary and necessary expense under I.R.C. Section 162 is per se unreasonable. Otherwise, regulations say little of what “reasonable compensation” is, other than the following:

- **Facts and circumstances.** A “facts and circumstances” test applies in determining whether the compensation for services or office space is “reasonable.” 29 C.F.R. § 2550.408c-2(b)(1); Treas. Reg. § 54.4975-6(e)(2).
- **Cannot duplicate full-time pay.** A plan may not compensate a disqualified person who receives full-time pay from an employer, an association of employers, or an employee organization whose employees or members are covered by a plan, except for reimbursement of direct expenses. 29 C.F.R. § 2550.408c-2(b)(2).
 - o **Limited.** This restriction applies only to plan fiduciaries, but not non-fiduciary parties in interest. Reimbursable direct expenses are those that would not have been incurred if the disqualified person

had not been rendering services to the plan (e.g., the reasonable cost of travel to and lodging during meetings of multiemployer plan trustees). No allocation of overhead costs may be included in the reimbursement. 29 C.F.R. §2550.408c-2(b)(3).

- o **Advances.** Expense advances are allowed if they are based on expenses expected to be incurred in the immediate future “such as during the next month” and are accounted for to the plan. 29 C.F.R. §2550.408c-2(b)(4).

- **Not “excessive compensation” under IRC rules.**

Compensation considered excessive under Treas. Reg. § 1.162-7 (relating to compensation for personal services which constitutes an ordinary and necessary trade or business expense) will not be “reasonable compensation.” 29 C.F.R. §2550.408c-2(b)(5).

- o Depending upon the facts and circumstances of the particular situation, compensation which is not excessive under Treasury regulations may, nevertheless, not be reasonable compensation within the meaning of ERISA §§ 408(b)(2) and 408(c)(2) (29 U.S.C. § 1108(b)(2), (c)(2)).

Mandatory Disclosures by Service Providers

The DOL has issued extensive disclosure requirements applying to service providers to pension plans if their arrangements with a plan are to be deemed a “reasonable arrangement.” Failure to make proper disclosures renders the arrangement “unreasonable”—and therefore a prohibited transaction—regardless of whether it is otherwise reasonable and complies with ERISA’s fiduciary standards. 29 C.F.R. §2550.408b-2(c)(1)(i). The most important consequence of inadequate disclosure is to expose the disqualified persons involved to prohibited transaction excise taxes. A plan fiduciary is exposed to both excise taxes and ERISA sanctions for its own failure to disclose.

Disclosure failures are not penalized if the service provider made a good faith, reasonably diligent effort to comply, and corrects any deficiency as soon as practicable (but in no case later than 30 days) after it is discovered. 29 C.F.R. §2550.408b-2(c)(1)(vii).

Plan Fiduciary Obligations

A plan fiduciary who engages a service provider that does not meet its disclosure obligation is deemed to have caused the plan to engage in a prohibited transaction, unless he or she was unaware of the failure and, after discovering it, does the following:

- The fiduciary requests the required disclosures, in writing.

- The fiduciary notifies the DOL if the service provider states that it will not comply or if it fails to comply within 90 days after the request. –and–
- If the service provider fails to comply by the end of the 90-day grace period, the fiduciary terminates the contract, unless doing so would be inconsistent with ERISA’s fiduciary standards. If the contract is for future services only, it must be terminated as expeditiously as is consistent with the fiduciary standards.

29 C.F.R. §2550.408b-2(c)(1)(ix).

A responsible fiduciary that didn’t take these steps would commit a prohibited transaction under ERISA (because he or she would have caused the plan to engage in nonexempt transaction with the service provider), though not under I.R.C. Section 4975 (because he or she would not himself or herself be the disqualified person that rendered the nonexempt services). Hence, the fiduciary wouldn’t be liable for Section 4975 excise tax but could, for instance, be required to reimburse the plan for any charges by the service provider in excess of reasonable compensation. The service provider would be exposed to excise tax liability.

For a further discussion on the service provider disclosure rules, see [Service Provider Disclosure Rules \(ERISA § 408\(b\)\(2\)\)](#).

Service providers must also furnish any other information about their compensation that the plan requests for purposes of completing an ERISA plan’s Form 5500 annual report. 29 C.F.R. §2550.408b-2(c)(1)(vi). The Section 408(b)(2) disclosure rules currently apply only to retirement plans, and not to employee welfare benefit plans, although the DOL has reserved the right to apply similar requirements in the future. 29 C.F.R. §2550.408b-2(c)(2).

Terminating Arrangements for Services or Office Space

A “reasonable arrangement” for services or office space must “permit termination by the plan without penalty to the plan on reasonably short notice under the circumstances to prevent the plan from becoming locked into an arrangement that has become disadvantageous.” The contract may, however, require the plan to compensate the service provider or lessor for actual losses that it suffers as a result of the early termination, such as the cost of maintaining and reletting office space that the plan has vacated. The provision must require the service provider or lessor to mitigate its damages. 29 C.F.R. §2550.408b-2(c)(2).

Provision of Services by Plan Fiduciaries or Related Persons

The DOL and IRS regulations make a point of emphasizing that selecting a service provider is a distinct transaction from furnishing services and that the statutory exemption covers only the latter. No protections are provided against allegations that, in making the choice of a provider, the responsible fiduciary engaged in self-dealing in violation of ERISA Section 406(a)(2). ERISA § 406(a)(2) (29 U.S.C. § 1106(a)(2)); 29 C.F.R. § 2550.408b-2(e)(1); Treas. Reg. § 54.4975-6(a)(5)(i).

Situations also may arise in which fiduciaries have relationships with service providers, which may be prohibited. Even factors other than relationships can affect a fiduciary's best judgment.

A fiduciary may select himself or herself or a person in whom he or she has an interest to perform services if no compensation is paid by the plan other than the reimbursement of direct expenses. 29 C.F.R. § 2550.408b-2(e)(3); Treas. Reg. § 54.4975-6(a)(5)(iii).

Distributions to Participants and Beneficiaries

Many individuals who are entitled to benefits under a plan are also parties in interest. For example, any officer, director, 10% shareholder, or active employee is a "party in interest" for purposes of ERISA § 406, and the first three categories plus a limited class of highly compensated employees are disqualified persons. On a literal reading of the statute, paying benefits to any of these would be a prohibited "transfer to . . . a party in interest, of any assets of the plan."

To avoid that unworkable outcome, ERISA provides an exemption for "[t]he making by a fiduciary of a distribution of the assets of the plan in accordance with the terms of the plan." Distributions on plan termination also must comply with the requirements of Title IV of ERISA (regarding terminations of PBGC-insured defined benefit plan). ERISA § 408(b)(9) (29 U.S.C. § 1108(b)(9)).

Distributions to Participants and Beneficiaries Who Are Plan Fiduciaries

ERISA also provides that Section 406(b)'s prohibition of self-dealing is not to be construed to prevent plan fiduciaries who are also participants from receiving benefits to which they are entitled "so long as the benefit is computed and paid on a basis which is consistent with the terms of the plan as applied to all other participants and beneficiaries." ERISA § 408(c)(1) (29 U.S.C. § 1108(c)(1)). Also see I.R.C. § 4975(d)(9).

Loans to Participants

Basic Conditions for Prohibited Transaction Exemption

A plan may lend money to parties in interest who are plan participants or beneficiaries if the loans:

- Are available to all participants or beneficiaries on a reasonably equivalent basis
- Are not made available to highly compensated employees (those defined as "highly compensated" under I.R.C. Section 414(q) for purposes of the qualified plan nondiscrimination standards) in an amount greater than the amount made available to other employees
- Are made in accordance with specific plan provisions
- Bear a reasonable rate of interest –and–
- Are adequately secured

ERISA § 408(b)(1) (29 U.S.C. § 1108(b)(1)); I.R.C. § 4975(d)(1).

If these conditions are satisfied, the participant's accrued benefit may be used as security for the loan, notwithstanding the general prohibition against the assignment, or alienation of benefits under ERISA § 206(d)(2) (29 U.S.C. § 1156(d)(2)) and I.R.C. § 401(a)(13)(A). The issues regarding plan loans to participants are discussed comprehensively in [Plan Loan Rules for Qualified Retirement Plans](#). For further plan loan resources, see [Plan Loan Resource Kit](#).

Banking Transactions

Three statutory exemptions permit transactions that would otherwise be prohibited between plans and banks or similar financial institutions that are supervised by federal or state authorities. The exempted transactions are:

- The deposit of plan funds with a bank or similar financial institution that is also a plan fiduciary or other party in interest
- The provision of ancillary services by a bank or similar financial institution that holds plan assets and is a fiduciary –and–
- A transaction between a plan and a common or collective trust fund maintained by a bank or trust company that is a party in interest

ERISA § 408(b)(4), (6), (8) (29 U.S.C. § 1108(b)(4), (6), (8)); I.R.C. § 4975(d)(4); 29 C.F.R. § 2550.408b-4, b-6; Treas. Reg. § 54.4975-6(b), (c). "Similar financial institution" is defined to include credit unions and savings and loan associations. The DOL has opined that other entities that

are licensed to engage in banking or trust activities and are subject to federal or state supervision are also eligible for these exemptions. ERISA Adv. Op. 96-15A (Aug. 7, 1996) (1996 ERISA LEXIS 27).

Bank Deposits

The exemption for bank deposits, which covers any temporary or permanent account that pays a “reasonable rate of interest,” including certificates of deposit, is available if either:

- The plan covers only employees of the bank and other members of the same controlled group, as defined in I.R.C. Section 414(b) or (c) –or–
- The investment is made by, or is made in accordance with an express authorization approved by, an unrelated fiduciary that has no interest in the bank that would affect its judgment
 - An authorization may be set forth in the plan, the trust agreement, or a separate instrument; but it must name the bank and state the authorization explicitly.

ERISA § 408(b)(4)(A), (B) (29 U.S.C. § 1108(b)(4)(A), (B)); I.R.C. § 4975(d)(4)(i); 29 C.F.R. § 2550.408b-4(b)(1), (2) (c)(2); Treas. Reg. § 54.4975-6(b)(2) and (b)(4)(ii). The exemption extends to all of the prohibitions in ERISA § 406(a) and the corresponding I.R.C. Section 4975 prohibitions, so that, for instance, a bank’s pension plan may place more than 10% of its assets in deposits with the bank, notwithstanding the general prohibition of ERISA § 407(a) on the acquisition by a plan of employer securities that are not qualifying employer securities. ERISA Opinion F-3641A (Jan. 22, 1988); ERISA Adv. Op. 79-76A (Oct. 31, 1979) (1979 ERISA LEXIS 16). However, the exemption does not include an exemption from the prohibitions under ERISA § 406(b) (3) (29 U.S.C. § 1106(b)(3)) and I.R.C. Section 4975(c)(1)(F), which prohibit fiduciaries from receiving consideration for their own benefit in connection with transactions involving plan assets. See ERISA Adv. Op. 2009-01A (Jan. 13, 2009) (2009 ERISA LEXIS 1).

Ancillary Services

The exemption for ancillary services connected with bank deposits permits a bank to make decisions to utilize its own services, which would ordinarily represent the use of plan assets by a fiduciary and its acting on behalf of a party (itself) with interests adverse to the plans, in violation of ERISA § 406(b)(1) and (2) (29 U.S.C. § 1106(b)(1), (2)). But, as with the deposit exemption, no relief exists from Section 406(b)(3), which prohibits parties dealing with the plan from receiving compensation. Neither the statute nor

the regulations define “ancillary services.” The DOL has stated, as a not-too-helpful generality, that an ancillary service is one that “aids or is auxiliary to a primary or principal service.” [ERISA Adv. Op. 2001-10 \(Dec. 14, 2001\)](#). The exemption is available only if the bank:

- Receives no more than reasonable compensation
- Has internal controls in place to ensure that the service is consistent with sound banking and financial practices –and–
- Performs the services in accordance with specific guidelines that preclude it from providing such ancillary service in an excessive or unreasonable manner and in a manner that would be inconsistent with the best interests of participants and beneficiaries

ERISA § 408(b)(6)(B) (29 U.S.C. § 1108(b)(6)(B)); I.R.C. § 4975(d)(6)(B); 29 C.F.R. § 2550.408b-6(b); Prohibited Transaction Class Exemption 82-63, 47 Fed. Reg. 14,804, 14,806 (April 6, 1982).

The DOL has also expressed its views regarding some specific services involving topics such as:

- Float income resulting from the short-term investment of the funds held in the account (Information Letter to Judith A. McCormick (Aug. 11, 1994) (1994 ERISA LEXIS 56))
- The moving of funds to satisfy current plan expenses into a noninterest-bearing account (29 C.F.R. § 2550.408b-6(a); Treas. Reg. § 54.4975-6(c)(1))
- Securities lending (Prohibited Transaction Class Exemption 81-6, 46 Fed. Reg. 7,527 (Jan. 23, 1981))
- Sweep services (Information Letter to Robert S. Plotkin, 1986 ERISA LEXIS 55 (Aug. 8, 1986) (1986 ERISA LEXIS 55))
- Overdraft protection ([Adv. Op. 2003-02A \(Feb. 10, 2003\)](#); ERISA Adv. Op. 79-73 (Oct. 11, 1979))

Common and Collective Trust Funds

A plan may purchase or sell units of a common or collective trust fund (or other pooled investment account) maintained by a bank or trust company that is a party in interest (such as a trustee) if:

- The bank or trust company is supervised by a state or federal agency
- The plan pays no more than reasonable compensation in connection with the transaction –and–
- The transaction is expressly permitted either by the terms of the plan or by a fiduciary that is independent of the bank and its affiliates

ERISA § 408(b)(8) (29 U.S.C. § 1108(b)(8)); I.R.C. § 4975(d)(8).

While DOL regulations have not been issued under this section, the DOL has stated in an advisory opinion that it considers the exemption to have the same scope as the other bank exemptions, that is, it exempts the bank from the prohibitions of ERISA §§ 406(a), 406(b)(1), and 406(b)(2) but not 406(b)(3). ERISA Adv. Op. 96-15A (1996 ERISA LEXIS 27).

Because the exemption is limited to purchases and sales of trust fund units, it doesn't exempt other transactions, such as those between a common trust fund and a plan investor's parties in interest other than the bank trustee. The DOL has issued a class exemption covering some of those transactions and clarifying the statutory exemption. See Prohibited Transaction Class Exemption 91-38, 56 Fed. Reg. 31,966 (July 12, 1991).

Transactions with Insurance Companies

Two exemptions for transactions between plans and insurance companies parallel the bank exemptions described in "Banking Transactions" above.

One exemption allows plans to buy and sell interests in pooled separate accounts maintained by insurance companies that are parties in interest. It is identical to (and included in the same statutory paragraph as) the exemption for bank common and collective trust funds. ERISA § 408(b)(8) (29 U.S.C. § 1108(b)(8)); I.R.C. § 4975(d)(8).

The other, more significant exemption allows plans to purchase annuity, health insurance, or life insurance contracts from insurance companies that are parties in interest, provided that the insurer is licensed to do business in one or more states and meets either of the following criteria:

- It is the employer that maintains the plan. –or–
- It is wholly owned by the employer or another party in interest and receives no more than 5% of its premium income from plans with respect to which it is a party in interest and its employers (not counting premiums for the insurer's own plans).

ERISA § 408(b)(5) (29 U.S.C. § 1108(b)(5)); I.R.C. § 4975(d)(5).

The purpose of this exemption was to make it possible for insurance companies to sell their own insurance products to their own plans and for employers that owned insurance companies to utilize their subsidiaries' products, provided that the subsidiary had a broad base of unrelated business. In practice, this narrow exemption did not prove to be

very useful. The DOL has since supplemented it with more expansive class exemptions. Prohibited Transaction Class Exemption 79-41, 44 Fed. Reg. 46,365 (Aug. 7, 1979); Prohibited Transaction Class Exemption 77-9, 42 Fed. Reg. 32,395 (June 24, 1977).

Purchases, Sales, or Leases of Employer Securities and Employer Real Property

As an exception to the prohibition against sales or leases of property between plans and parties in interest, a plan may acquire "qualifying employer securities" from, or sell them to, a party in interest. It may also acquire, sell, or lease "qualifying employer real property." Holding employer securities or employer real property that are not "qualifying" is absolutely forbidden. ERISA § 407(a)(1) (29 U.S.C. § 1107(a)(1)); I.R.C. § 4975(d)(8).

Three general conditions apply to the exemptions:

- The plan may pay no more than "adequate consideration" (i.e., fair market value) for the property and may not sell or lease it for less than adequate consideration.
- No commission may be charged on the transaction.
- Unless the plan is an "eligible individual account plan," its holding of employer securities and employer real property after any acquisition must not exceed 10% of the total value of plan assets.

ERISA §§ 407(a)(2), 408(e)(1), (2), (3) (29 U.S.C. §§ 1107(a)(2), 1108(e)(1), (2), (3)); I.R.C. § 4975(d)(11), (13).

A key use of the exemption for the acquisition of employer securities is to enable corporations or their shareholders to sell employer stock to employee stock ownership plans (ESOPs). If, in connection with the sale, the plan borrows from, or on the guarantee of, the employer or another party in interest, the loan also must comply with the statutory exemption for loans to ESOPs. ERISA § 408(b)(3) (29 U.S.C. § 1108(b)(3)); I.R.C. § 4975(d)(3). For more information on this topic, see [Employee Stock Ownership Plan Design and Compliance](#) and [Employer Securities and Real Property ERISA Investment Rules](#). For an additional discussion on the topic, see Lexis Tax Advisor -- Federal Topical § 1C:19.05, paragraph [7].

Plan Transactions with Investment Advisers and Advice Arrangements

Under regulations issued in 1975 (1975 Regulation), which remain in effect today after subsequent regulations issued in 2016 (2016 Regulation) were vacated by the Fifth Circuit Court of Appeals in *Chamber of Commerce of the United States v. U.S. Department of Labor*, 885 F.3d 360 (5th Cir.

2018), a person is considered to be rendering investment advice to a plan if the following five-part test is met:

- The person gives advice to the plan as to the value of securities or other property, or makes a recommendation as to the advisability of investing in, purchasing, or selling securities or other property.
- The person regularly provides this type of advice to the plan.
- The person has an agreement, arrangement, or understanding, written or otherwise, with a plan fiduciary to provide this advice.
- The advice will serve as a primary basis for investment decisions with respect to plan assets.
- The advice will be individualized based on the particular needs of the plan.

Under this rule, investment advisers who play a role in shaping plan investments may or may not be considered fiduciaries under ERISA depending on whether or not they meet the five-part test described above. 29 C.F.R. § 2510.3-21, as published in 40 Fed. Reg. 50,842 (Oct. 31, 1975); 85 Fed. Reg. 40,834 (July 7, 2020) (notice of proposed class exemption); 85 Fed. Reg. 40,589 (July 7, 2020) (implementing the vacatur of the DOL's 2016 final rule defining who is a fiduciary under ERISA and reflecting the removal of PTE 2016-01 and PTE 2016-02).

Investment advisers with respect to IRAs and other individual arrangements covered under I.R.C. Section 4975 have historically **not** been considered ERISA fiduciaries under the 1975 Regulation five-part test, in part, because neither ERISA nor the 1975 Regulation treats such arrangements as "plans." The IRC's definition of fiduciary in regulations implementing its prohibited transaction rules, which is nearly identical to the 1975 Regulation's, refers to "employee benefit plans" without defining the term. Treas. Reg. § 54.4975-9(c)(1).

Since the 1975 Regulation, substantially more retirement income has been invested in participant-directed investments (such as in 401(k) plans and IRAs). As a result, investment advisers have become increasingly susceptible to conflicts of interest and self-dealing when providing investment advice to plan participants (directly and indirectly) and to IRA owners. For example, an investment adviser may recommend a certain mutual fund to a plan or an IRA owner as an investment option when the adviser has a commission arrangement with the mutual fund manager. In this arrangement, the adviser earns a fee if a threshold amount of assets is directed to the fund based on the adviser's advisory services to its clients.

Investment Advice Fiduciary Regulations and PTE 2020-02

Note that the following section may change in the near future due by the Biden Administration. The DOL has stated that as of January 20, 2021, the information provided in its news releases may be out of date or not reflect current policies. [DOL news release](#).

On June 29, 2020, the DOL announced new guidance on the investment advice fiduciary rule. See [EBSA News Release](#). Here, the DOL proposed a new prohibited transaction class exemption for investment adviser fiduciaries, the final version of which was issued in late 2020. See Prohibited Transaction Exemption 2020-02, 85 Fed. Reg. 82,798 (Dec. 18, 2020), discussed below. In addition, the DOL issued a technical amendment to 29 C.F.R. § 2510-3.21 to reinstate the 1975 regulations on investment advice fiduciaries and Interpretive Bulletin 96-1 relating to participant investment education, effective on July 7, 2020. See 85 Fed. Reg. 40,589 (July 7, 2020).

Under ERISA and the IRC, a person is a fiduciary if he or she renders investment advice for a fee or other compensation. ERISA § 3(21)(A)(ii), I.R.C. § 4975(e)(3)(B). If the adviser meets the five-part test and receives fees, he or she will be deemed an investment adviser fiduciary under ERISA and the IRC. For more on this topic, see [DOL Finalizes Fiduciary Investment Advice Guidance](#).

As cited above, the DOL finalized proposed prohibited transaction class exemption (PTE 2020-02) on December 18, 2020, allowing registered investment advisers, broker-dealers, insurance companies, and banks to receive compensation for providing fiduciary investment advice (including advice to roll over plan assets to IRAs) and to engage in principal transactions involving the purchase and sale of their (and their affiliates') proprietary investment products, so long as certain conditions are met. 85 Fed. Reg. 82,798 (Dec. 18, 2020).

The exemption is effective February 16, 2021, and the DOL announced that Field Assistance Bulletin 2018-02 (FAB 2018-02) will remain in effect until December 20, 2021, to provide parties with a transition period to comply with the new exemption. The DOL will not pursue prohibited transaction claims against investment advice fiduciaries who attempt to comply in good faith with the impartial conduct standards, which include a best interest standard, a reasonable compensation standard, and a requirement to make no misleading statements about investment transactions and other relevant matters. 85 Fed. Reg. 82,799 (Dec. 18, 2020).

Key aspects of PTE 2020-02 include the following:

- Advisers are subject to a best interest standard, involving duties of prudence and loyalty, and the advice may not contain materially misleading statements.
- Compensation received for the advice must be reasonable.
- The person giving the advice must regularly provide the same type of advice.
- Advice regarding rollovers from a plan must be accompanied by documentation giving the specific reasons of the recommendations.
- The financial institution must also:
 - Disclose its status as an investment advice fiduciary under ERISA and the IRC, as applicable, and provide a description of its services and material conflicts of interest
 - Establish, maintain, and enforce policies and procedures prudently designed to ensure compliance with the impartial conduct standards –and–
 - Conduct an annual review to detect and prevent violations
- Financial institutions or investment professionals with certain criminal convictions or egregious noncompliance with the exemption could result in ineligibility for a period of 10 years.
- The DOL does not intend that the fiduciary acknowledgment or any of the disclosure obligations create a private right of action beyond those expressly provided by statute, such as in ERISA Section 502(a) and I.R.C. Section 4975.

85 Fed. Reg. 82,798 (Dec. 18, 2020).

The preamble to PTE 2020-02 acknowledges certain circumstances where the 1975 Regulation fiduciary definition could encompass investment advice relating to IRAs and other individual investment arrangements. In any event, the five-part test would need to be met. For example, a one-time interaction where a retiring participant obtains advice regarding the rollover of a lump-sum distribution but had not received any other advice from the adviser would not constitute investment advice since the second prong of the test is not met.

PTE 2020-02 does not cover advice arrangements that rely only upon robo-advice without any interaction with an investment professional (which would be covered under ERISA's statutory exemption for eligible advice arrangements under Section 408(b)(14) (discussed below)). However, PTE 2020-02 **would** cover “hybrid” robo-advice arrangements involving advice that is generated by

computer models in connection with additional interaction from an investment professional.

See [DOL Fact Sheet: Improving Investment Advice for Workers & Retirees](#) for more information on the 2020 Regulation and PTE 2020-02.

Exemption for Certain Eligible Advice Arrangements under ERISA Section 408(b)(14)

The Pension Protection Act of 2006 (Pub. L. No. 109-280, §601) added a prohibited transaction exemption designed to alleviate concerns that furnishing investment advice to participants and using plan assets to compensate the adviser might run afoul of the prohibited transactions rules if the adviser also executed the transactions that it had recommended. ERISA §408(b)(14), (g) (29 U.S.C. §1108(b)(14), (g)); I.R.C. §4975(d)(17), (f)(8); 29 C.F.R. §§2550.408g-1, 2550.408g-2. However, this exemption is limited to certain arrangements that meet very specific criteria.

Specifically, the exemption provides that no prohibited transaction takes place if, in accordance with an “eligible investment advice arrangement”:

- An adviser renders investment advice (as described in ERISA § 3(21)(A)(ii) (29 U.S.C. § 1002(21)(A)(ii))) to participants or beneficiaries
- The recipient of the advice makes investment decisions for his or her plan account in reliance on it –and–
- The adviser receives direct or indirect compensation from plan assets for the advice itself or for executing transactions directed by participants in reliance on the advice

ERISA §408(b)(14)(A) (29 U.S.C. §1108(b)(14)(A)); I.R.C. §4975(d)(17)(A). The criteria for an eligible investment advice arrangement are as follows:

- The adviser must be one of the following:
 - An adviser registered under the Investment Advisers Act of 1940 or under a comparable law of the state in which it maintains its principal office and place of business
 - The trust department of a bank or savings association subject to periodic examination by federal or state authorities
 - An insurance company qualified to do business in at least one state
 - A registered broker or dealer –or–
 - An affiliate of one of the foregoing (ERISA §408(g)(11)(A) (29 U.S.C. §1108(g)(11)(A)); I.R.C. §4975(f)(8)(J)(i))

- The investment advice arrangement must be expressly authorized by a plan fiduciary other than the adviser, entities that offer investment options under the plan, or their affiliates. The plan sponsor and the fiduciaries who authorize the arrangement are not liable for advice provided under the arrangement and have no obligation to monitor it, but they are obliged to select the adviser prudently and to review the arrangement periodically. ERISA §408(g)(4), (10) (29 U.S.C. §1108(g)(4), (10)); I.R.C. §4975(f)(8)(D); 29 C.F.R. §2550.408g-1(b)(5).
- Unless the advice is generated by a computer model (see below), the adviser's compensation and the compensation of its employees, agents, or registered representatives "(including commissions, salary, bonuses, awards, promotions, or other things of value)" must not vary, directly or indirectly, on the basis of the participant's investment decisions. The imposition of this "fee leveling" condition not only upon the adviser's personnel but also on their employer greatly lessens the exemption's usefulness. ERISA §408(g)(2)(A)(i) (29 U.S.C. §1108(g)(2)(A)(i)); I.R.C. §4975(f)(8)(B)(i)(I); 29 C.F.R. §2550.408g-1(b)(3)(D).
- The adviser must request information "relating to age, time horizons (e.g., life expectancy, retirement age), risk tolerance, current investments in designated investment options, other assets or sources of income, and investment preferences of the participant or beneficiary" and must utilize it to the extent that it is provided. (The participant is under no obligation to respond to the request.) Advice must be "based on generally accepted investment theories" and must take fees and expenses into account. 29 C.F.R. §2550.408g-1(b)(3), (A), (B), (C).
- Advice generated by certified computer models is exempt from the fee leveling compensation restrictions that would otherwise apply. The statute and regulations prescribe standards that a model must satisfy and require that compliance be certified by a qualified expert before the model is used to offer recommendations. ERISA §408(g)(2)(A)(iii), (3) (29 U.S.C. §1108(g)(2)(A)(iii), (3)); I.R.C. §4975(f)(8)(B)(i)(II), (C); 29 C.F.R. §2550.408g-1(b)(4).
- The arrangement must comply with disclosure, compliance audit, and record maintenance requirements not detailed here. ERISA §408(g)(5)–(9) (29 U.S.C. §1108(g)(5)–(9)); I.R.C. §4975(f)(8)(E)–(I); 29 C.F.R. §2550.408g-1(b)(6).

The exemption also covers the adviser's employees, agents, and registered representatives.

Block Trades

Investment managers commonly acquire or dispose of the same securities simultaneously for multiple clients by

purchasing or selling a block of shares through a single broker-dealer. Where the manager's client is an ERISA plan, the broker-dealer may be a party in interest for one or more of them. Rather than compel managers to split transactions among different broker-dealers (perhaps resulting in higher costs), a statutory exemption applies. ERISA §408(b)(15) (29 U.S.C. §1108(b)(15)); I.R.C. §4975(d)(18).

To qualify for the exemption, the block must consist of at least 10,000 shares or have a market value of at least \$200,000. ERISA §408(b)(15)(B) (29 U.S.C. §1108(15)(B)); I.R.C. §4975(f)(9). The following conditions must also be satisfied:

- No particular employer's plans may buy or sell more than 10% of the block.
- The terms of the transaction must be no less favorable to the plans than if the purchases or sales were at arm's length.
- Commissions may not exceed those that would be charged for an arm's-length transaction.
- The party in interest that executes the transaction may not be a fiduciary of any of the plans by reason of its authority or control over plan assets.

ERISA §408(b)(15)(A) (29 U.S.C. §1108(15)(A)); I.R.C. §4975(d)(18). The last condition was presumably intended to prevent the manager from executing the trade through its own affiliates.

Trades Executed through Alternative Trading Systems

In trades on traditional stock exchanges, the parties do not know, and would have great difficulty discovering, one another's identity. For that reason, there is no need to be concerned about whether a plan might inadvertently buy shares from, or sell them to, a party in interest. DOL ERISA Adv. Op. 92-23A (Oct. 27, 1992).

In a 2004 advisory opinion, the DOL considered whether the same reasoning applied to an electronic trading system utilized by institutional investors. The system allowed anonymous negotiation of securities transactions, though nothing prevented parties from identifying themselves to their counterparties. The DOL opined that transactions between plans and parties in interest wouldn't be prohibited so long as the parties didn't know that parties in interest were involved. DOL ERISA Adv. Op. 2004-05A (May 24, 2004).

Additionally, a statutory exemption exempts purchases or sales of securities "through an electronic communication

network, alternative trading system, or similar execution system or trading venue” that is subject to U.S. government regulation. The DOL has the authority to issue regulations expanding the exemption to purchases or sales of other property and to systems regulated by foreign governments, though it has so far done neither. ERISA §408(b)(16)(A) (29 U.S.C. § 1108(16)(A)); I.R.C. § 4975(d)(19)(A).

The following conditions must be met for the exemption to apply:

- Either:
 - The trade is executed in accordance with “rules designed to match purchases and sales at the best price available through the execution system” –or–
 - Neither the system nor any of the parties identify the buyers and sellers
- The price and commissions do not exceed those of an arm’s-length transaction.
- If a party in interest to a plan owns or partly owns the system and utilize it for its own trades, the plan’s use of the system is authorized by the plan sponsor or by a fiduciary that is independent of the party in interest.
 - The system owner must notify the plan sponsor or the authorizing fiduciary of its intention to use the system at least 30 days before the first trade is executed.

ERISA §408(b)(16) (29 U.S.C. §1108(16)); I.R.C. §4975(d)(19). Two noteworthy points are (1) that the exemption may be available even when a plan knows that it is trading with a party in interest, so long as impartial rules set the terms of the transaction and (2) that a system in which a plan fiduciary has an ownership interest may be utilized if approved by another fiduciary or the plan sponsor.

Transactions between Plans and Service Providers

Persons who are parties in interest (other than fiduciaries) solely because they provide services to a plan (which, in itself, is prohibited under ERISA §406) may engage in transactions with the plan that would otherwise be prohibited (like purchases, sales, or leases of assets, loans, and use of plan assets) so long as the terms are no less favorable to the plan than “adequate consideration.” ERISA §408(b)(17) (29 U.S.C. § 1108(17)); I.R.C. § 4975(d)(20). Adequate consideration is defined within the statute. ERISA §408(b)(17)(B) (29 U.S.C. § 1108(17)(B)); I.R.C. § 4975(d)(20)(B).

The same exemption extends to persons who are parties in interest solely by reason of their relationships to a non-

fiduciary service provider (members of an individual service provider’s family, companies in which a service provider has a 50% or greater ownership interest, or officers, directors, employees, or 10% shareholders of a service provider). ERISA §408(b)(17)(A) (29 U.S.C. § 1108(17)(A)); I.R.C. § 4975(d)(20)(A).

The rationale for this exemption is that transactions with non-fiduciary service providers must, by definition, be negotiated with plan fiduciaries and therefore entail little risk for the plan.

Foreign Exchange Transactions

Plans that invest in foreign securities frequently need to convert dollars into or out of pounds, euros, yen, renminbi, or more exotic currencies. Often the simplest and most economical way to do this is to make use of the plan’s trustee, custodian, or broker. The obstacle, of course, is that those fiduciaries or service providers are parties in interest, and currency is an asset that parties in interest are prohibited from selling to, or buying from, the plan.

The DOL promulgated prohibited transaction class exemptions to facilitate currency conversions. Prohibited Transaction Class Exemption 94-20, 59 Fed. Reg. 8,022 (Feb. 17, 1994) and Prohibited Transaction Class Exemption 98-54, 63 Fed. Reg. 63,503 (Nov. 13, 1998). A broader statutory exemption now exists.

That exemption is available for foreign exchange transactions between plans and banks, broker-dealers, or their affiliates “in connection with the purchase, holding, or sale of securities or other investment assets (other than a foreign exchange transaction unrelated to any other investment in securities or other investment assets).” ERISA §408(b)(18)(A) (29 U.S.C. § 1108(b)(18)(A)); I.R.C. § 4975(d)(21)(A). The exemption covers exchanges to facilitate purchases, sales, dividend and interest payments, hedging, and the like, but not currency speculation. The following conditions must be satisfied:

- The plan’s counterparty may not have investment discretion or render investment advice concerning the transaction.
- The terms of the transaction must be no less favorable to the plan than those that the counterparty would offer in a comparable arm’s-length transaction with an unrelated party.
- The exchange rate for the transaction may be no more than 3% (**not** percentage points!) higher or lower than “the interbank bid and asked rates for transactions of comparable size and maturity at the time of the transaction as displayed on an independent service.”

ERISA §408(b)(18) (29 U.S.C. §1108(b)(18)); I.R.C. §4975(d)(21).

Cross Trading

Investment managers frequently reduce transaction costs by having one of their managed accounts purchase securities from another account instead of on the market, a technique known as “cross trading.” If one of the accounts is an ERISA plan, that transaction places the manager in the position of acting for a party with interests adverse to the plan, in violation of ERISA §406(b)(2). In some instances, too, the other account may be a party in interest with respect to the ERISA account, resulting in a prohibited sale of assets between the plan and a party in interest.

A statutory exemption permits cross-trades, subject to these conditions:

- The transaction must be a cash sale of “a security for which market quotations are readily available.”
- The price must be the security’s “current independent market price,” as determined under 17 C.F.R. §270.17a-7(b), which provides rules for determining the market price of securities whose prices are reported in various ways, ranging from the “pink sheets” to major stock exchanges.
- No brokerage commissions or other fees, other than customary transfer fees, may be paid by the parties to the transaction.
- The ERISA plans involved in the transaction must have assets of at least \$100 million, or its assets must be held in a master trust with assets of at least \$100 million.
- A fiduciary unrelated to the investment manager must give the manager authorization in advance to engage in cross trading.
- The investment manager must not base its fee schedule or the availability of any of its services on the plan’s consent to cross trading.
- The investment manager must establish “written cross-trading policies and procedures that are fair and equitable to all accounts participating in the cross-trading program.” It must also designate an individual to review its compliance with the written policies and issue an annual report to the plan fiduciary who authorized cross trading.
- The investment manager must provide a quarterly report to the authorizing fiduciary, disclosing all of the plan’s cross-trades and the method used to derive the price at which they were executed.

ERISA §408(b)(19) (29 U.S.C. §1108(b)(19)); I.R.C. §4975(d)(22); 29 C.F.R. §2550.408b-19.

Other Statutory Exemptions

Several additional statutory exemptions exist. Some simply ensure that conformity to other ERISA requirements will not be characterized as a prohibited transaction. The following is a summary:

- The distribution of assets on plan termination in accordance with the terms of the plan and the requirements of ERISA is exempt. ERISA §408(b)(9) (29 U.S.C. §1108(b)(9)); I.R.C. §4975(d)(12).
- Any transaction required or permitted by ERISA’s special provisions for multiemployer plans (ERISA §§4201 through 4303) is exempt with the proviso (implicit in the ERISA and explicit in the IRC) that the exemption does not extend to a plan fiduciary’s self-dealing or improper receipt of consideration from parties dealing with the plan. ERISA §408(b)(10) (29 U.S.C. §1108(b)(10)); I.R.C. §4975(d)(14).
- Mergers of, or transfers of assets or liabilities between, multiemployer plans with the same caveat as in the preceding exemption are exempt. See ERISA §408(b)(11) (29 U.S.C. §1108(b)(11)).
- Included is an exemption from the prohibition against representing a party dealing with the plan (so that trustees who serve on the boards of both parties to the merger may participate in negotiating its terms). ERISA §408(f) (29 U.S.C. §1108(f)) (no corresponding IRC provision).
- Transfers of excess pension plan assets to a retiree health account in accordance with I.R.C. Section 420. ERISA §408(b)(13) (29 U.S.C. §1108(b)(13)); I.R.C. §420(a)(3)(B).

Exemptions for Plans Holding Employer Stock

The following exemptions are designed to address narrow problems that may be encountered by plans that hold stock of the plan sponsor or other parties in interest:

- Exercising the right to convert a security (e.g., of preferred stock to common) is technically an exchange but is permitted so long as the plan receives securities of equivalent value. ERISA §408(b)(13) (29 U.S.C. §1108(b)(13)); I.R.C. §420(a)(3)(B).
- If a plan holds shares of employer stock that cease to be qualifying employer securities, it may sell them to a party in interest, so long as the sale is for adequate consideration (i.e., fair market value) and no commission is charged. ERISA §408(b)(13) (29 U.S.C. §1108(b)(13)); I.R.C. §420(a)(3)(B). For example, employer stock held by a plan other than an eligible individual account plan loses its qualifying employer security status if persons independent of the issuer no longer hold at least 50% of

that class of stock (e.g., as the result of a “going private” transaction). ERISA § 408(b)(13) (29 U.S.C. § 1108(b)(13)); I.R.C. § 420(a)(3)(B).

- Without the exemption, the plan would be compelled to sell its shares to an unrelated party.

Exemption for IRA Owners

Another exemption exists for sales by IRAs to their owners of bank stock that the IRA is no longer permitted to hold after the bank’s election of Subchapter S status. This exemption is available only if the IRA held the stock on October 22, 2004. I.R.C. § 4975(d)(16).

Authority to Grant Exemptions

ERISA directs the DOL to “establish an exemption procedure” under which “[the Secretary] may grant a conditional or unconditional exemption of any fiduciary or transaction, or class of fiduciaries or transactions, from all or any part of the restrictions imposed by sections 406 and 407(a).” ERISA § 408(a) (29 U.S.C. § 1108(a)). A parallel provision directs the secretary of the treasury to establish a similar procedure for administrative exemptions from the Internal Revenue Code’s prohibited transactions rules. I.R.C. § 4975(c)(2). Exemptions under each procedure are to be granted only if they are:

- 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

ERISA § 408(a) (29 U.S.C. § 1108(a)); I.R.C. § 4975(c)(2). The statute includes some general procedural requirements:

- Proposed exemptions must be published in the Federal Register.
- Interested persons must be given an adequate notice and an opportunity to present their views.
- An opportunity must be given for a hearing.
- Findings must be made on the record to show that the conditions for granting the exemption are met.

I.R.C. § 4975(c)(2). The DOL has sole authority to issue exemptions, including those for individual retirement accounts and other plans that are subject to the prohibitions of the IRC but are exempt from ERISA.

Exemptions fall into two broad classes:

- **Individual exemptions.** These apply only to the transaction for which they are requested and to the persons who are identified as parties to the transaction.

The DOL has published a list of granted and proposed individual exemptions [here](#) in its Index of Granted Individual Exemptions.

- o “EXPRO” exemptions (discussed below) are individual exemptions granted under an expedited procedure. The applicant must demonstrate only that its transaction is substantially similar to two or more transactions for which the DOL has previously granted individual exemptions and that it presents little risk of abuse or of loss to the plan participants. The DOL has published a list of approved EXPRO exemptions [here](#) in its Index of Approved EXPRO Authorizations.

- **Class exemptions.** These apply to categories of transactions. The DOL has published a list of granted and proposed class exemptions [here](#).

29 C.F.R. § 2570.31(e).

Individual Exemptions

The DOL is authorized to grant administrative exemptions on either an individual or a class basis from the restrictions of ERISA Sections 406 and 407 on meeting the conditions indicated in the section above. Individuals and other parties to a prospective transaction should apply to the DOL for a determination that the identified transaction or performance of services is eligible for an exemption from the prohibited transaction rules. The DOL sets forth an application process at its [website for Individual Exemptions](#).

Applications for Individual Exemptions

Plans (through their plan administrators or counsel) should apply for individual exemptions prior to engaging in the transaction with any party whose participation in it is prohibited. 29 C.F.R. § 2570.32(a). While applications should be filed before the transaction takes place, retroactive exemptions are possible (although disfavored) unless an investigation of the transaction or of the parties participating in it is pending. Individual applications will be returned or placed on hold if a substantially similar class exemption is pending on which the DOL expects to take action in the reasonably near future. 29 C.F.R. § 2570.33(a).

There is no prescribed form for applications, only a list of subjects that must be covered, thus provide:

- A full description of the transaction
- An explanation of why it meets the statutory standards for exemption grants
- The information about the plan and about past

investigations, lawsuits or criminal convictions involving it, or the parties to the transaction –and–

- Where the transaction has already taken place, the reasons for engaging in it before obtaining an exemption must be explained (The DOL rarely grants retroactive exemptions.)

Because the exercise of determining who is an “interested person” depends on the facts and circumstances for a particular transaction, there may be instances where the notice must be sent to persons other than participants and beneficiaries. See [DOL, 29 CFR 2570 Prohibited Transaction Exemption Procedures Employee Benefit Plans](#).

For a practical guidance checklist to guide you in developing a PTE application, see [Prohibited Transaction Exemption Application Checklist](#).

Notice to Interested Persons

The applicant is required to send interested persons a copy of the proposed exemption, accompanied by a statement (which can be copied verbatim from the regulation) regarding their right to submit comments. 29 C.F.R. §2570.43(a).

Notice Delivery

The method of providing the notice “must be reasonably calculated to ensure that interested persons actually receive the notice.” Email or use of a website is permitted if the applicant “provide[s] satisfactory proof of electronic delivery to the entire class of interested persons.” 29 C.F.R. § 2570.43(b).

Preparing a Notice Summary for Distribution

The DOL may also require the applicant to prepare and distribute a summary of the proposed exemption. The summary should explain:

- The nature of the transaction
- Why the transaction is prohibited
- Why the plan seeks to undertake the transaction –and–
- What conditions and safeguards will be established to protect the interests of the plan and its participants

Prepare the summary so that it is “written in a manner calculated to be understood by the average participant.” The DOL must approve the summary before it is distributed.

29 C.F.R. § 2570.43(d).

The PTE applicant must submit a declaration under penalties of perjury verifying that notifications have been

provided. Without that declaration, an exemption will not be granted. 29 C.F.R. § 2570.43(c).

Pendency of the Application

Applicants are required to notify the DOL of any material changes of fact while their applications are pending. 29 C.F.R. § 2570.37(a). The DOL must also be notified if the applicant or any party in interest that will participate in the transaction becomes the subject of a DOL, IRS, PBGC, or Justice Department investigation or enforcement action relating to ERISA or the employee benefit provisions of the Internal Revenue Code. 29 C.F.R. § 2570.37(b).

Request for a Public Hearing by Any Interested Person

If a proposed exemption would grant relief from the prohibitions against self-dealing by fiduciaries, any interested person who will be adversely affected may request a public hearing. The DOL will grant the request if it determines “a hearing is necessary to fully explore material factual issues identified by the person requesting the hearing.” ERISA §406(b) (29 U.S.C. §1106(b)); I.R.C. § 4975(c)(1)(E), (F); 29 C.F.R. § 2570.46.

The DOL may also schedule hearings on its own initiative. 29 C.F.R. § 2570.47(a). Exemption applicants must:

- Notify interested persons of any hearing in a manner satisfactory to the DOL –and–
- Submit a statement under penalties of perjury confirming that the notification has been given

29 C.F.R. §§ 2570.46(c), (d), 2570.47(b).

Publication of Approved Exemption

Once it reviews comments to a PTE exemption request and possibly conducting hearings, the DOL will either (1) publish a Federal Register notice approving the exemption or (2) issue a final denial letter. 29 C.F.R. §§ 2570.48(b), 2570.41(c). For a sample exemption approval, see 81 Fed. Reg. 72,114 (Oct. 16, 2014).

Withdrawal, Reconsideration, and Revocation

An applicant that receives a final denial letter may request reconsideration within 180 days after the denial. The request must be based on “significant new facts or arguments [that], for good reason, could not have been submitted for the Department’s consideration during its initial review of the exemption application.” 29 C.F.R. § 2570.45.

Applications may be withdrawn at any point during the approval process. A withdrawn application may be

reinstated, and the DOL will then resume its review. 29 C.F.R. § 2570.45.

The DOL retains the right to revoke or modify exemptions after publishing a notice of the proposed action in the Federal Register and giving the applicant an opportunity to comment. Revocations and modifications ordinarily are prospective. An exemption for a continuing transaction, such as a lease, may become ineffective if there is a material change of pertinent facts or if the conditions for the exemption cease to be satisfied. 29 C.F.R. §§ 2570.49, 2570.50.

Application for Class Exemptions

The procedure for granting class exemptions parallels that for individual exemptions, with the following differences:

- An association or organization representing parties in interest who may be parties to the exemption transaction can apply for a class exemption, as individual plans can, or parties in interest. See, e.g., 66 Fed. Reg. 33,185 (June 3, 2003) (Proposed Class Exemption for Acquisition and Sale of REIT Shares by Individual Account Plans Sponsored by Trust REITS); 29 C.F.R. § 2570.32(a)(3).
- The DOL has proposed class exemptions on its own motion, or after receiving several applications for similar individual exemptions. See, e.g., Proposed Class Exemption for Cross-Trades of Securities by Index and Model-Driven Funds, 64 Fed. Reg. 70,057 (Dec. 15, 1999).

Applications need not include information that is pertinent only to individual exemptions.

Persons who rely on a class exemption are not required to notify the DOL or take any other formal action. They need only to satisfy the conditions for the exemption. If there is doubt on that score or the conditions cannot be met precisely, the prudent course of action is to request an individual exemption.

Granted Class Exemptions

For a list of class exemptions granted by the DOL, see [DOL, Granted Class Exemptions](#).

EXPRO (Expedited Processing) Applications for Exemption

The DOL has established a program that streamlines the exemption process for transactions involving very similar facts where the conditions on which they are granted tend to be virtually identical. They are not, however, suitable for class exemptions, because they require some scrutiny to minimize the risk of abuse. This is the DOL's EXPRO (for "expedited processing") program which makes it possible to obtain an exemption without engaging in the formalities of Federal Register notice and without the delays inherent in the standard procedure. For EXPRO to apply, the facts of the transaction must be substantially the same as for two or more transactions for which the DOL has granted individual exemptions in the recent past.

EXPRO Eligibility

A transaction is eligible for an EXPRO exemption if it is substantially similar to either:

- Two transactions for which the DOL has granted individual exemptions during the 60-month period ending of the date of the application for the exemption –or–
- One EXPRO exemption granted during the past 60 months and one individual exemption granted during the past 120 months

The determination of whether transactions are "substantially similar" is within the sole discretion of the DOL. The EXPRO application process was established by the DOL as published in a Federal Register as an expansion of an earlier exemption procedure. See 61 Fed. Reg. 39,988 (July 31, 1996), as amended by 66 Fed. Reg. 44,622 (July 3, 2002) (PTE 96-62). EXPRO authorizations, by year, are listed at [DOL, EXPRO Authorizations under PTE 96-62](#). The website contains a list of exemptions granted to date under the EXPRO program indexed by the type of transaction, like:

- In-Kind Redemptions by Plans of Mutual Fund Shares
 - Lease by Plan of Real Property
 - Loan by Plan
 - Purchases by Plans of Real Property
 - Sales by Plans/IRAs of Employer Securities
 - Sales by Plans of Real Property
-

The entry for each exemption shows which prior exemptions the applicant relied on and, with a few exceptions, includes a link to a copy of the notice to interested persons.

Preparing the EXPRO Application

An EXPRO application must be filed and approved before the transaction takes place. The application must include:

- All information required in an application for an individual prohibited transaction exemption
- A demonstration “that the proposed transaction poses little, if any, risk of abuse or loss to the plan participants and beneficiaries”
- A comparison to the previous exemptions that form the predicate for EXPRO eligibility –and–
- A draft of the required notice to interested persons and a description of how it will be distributed to them

PTE 96-62, § III(a).

If either of the predicate exemptions was conditioned on engaging the services of an independent fiduciary, the same condition applies to the EXPRO exemption.

An independent fiduciary must conduct a review of the following related to the proposed exemption:

- It must review the proposed transaction.
- It must determine that it is in the best interests of the participants.
- It must represent their interests when the transaction is carried out and, in the case of a continuing transaction (e.g., a lease of property to or from a party in interest), represent their interests.
- It must enforce compliance with the conditions of the exemption. –and–
- Otherwise ensure that the transaction remains in their best interests throughout its continuance.

PTE 96-62, § III(b).

Prepare an EXPRO application to include the following:

- Identify the independent fiduciary.
- Include a statement by the independent fiduciary explaining why the transaction is in the participants’ best interests and its agreement to represent their interests. –and–
- Describe the procedure for replacing the independent fiduciary, if necessary.

PTE 96-62, § III(b).

DOL Tentative Authorization

The transaction is tentatively authorized if the DOL either:

- Issues a written determination that the submission meets the conditions for authorization –or–
- Fails to respond to the application within 45 days after acknowledging its receipt

PTE 96-62, § IV(c).

After receiving tentative authorization, the applicant must distribute a notice to interested persons. Similar to the notice required for individual exemptions (see Individual Exemptions above), the notice to interested persons should:

- Describe the proposed transaction, stating that a tentative exemption has been issued
- Furnish citations to the prior exemptions on which the application relies –and–
- Advise the recipients of their right to submit comments to the DOL

PTE 96-62, §§ III (d), IV(b). The comment period ends 25 days after the distribution of the notice is completed. First-class mail is presumed to take 3 days to arrive, so that, if notice is given in that way, the comment period ends 28 days after the date of mailing. PTE 96-62, § IV(e).

Final authorization of the exemption occurs five days after the end of the comment period, unless the DOL determines:

- That the exemption should not be granted –or–
- “Substantive adverse comments” are received

In the latter case, the applicant must resolve the issues raised by the comments to the DOL’s satisfaction before the final authorization will be issued.

José M. Jara, Counsel, Fox Rothschild LLP

José M. Jara's practice focuses on ERISA and employment litigation and counseling and includes representing clients under investigation by the Department of Labor ("DOL") and Employee Benefits Security Administration ("EBSA"), and defending clients from lawsuits filed by the DOL's Office of the Solicitor regarding civil and/or criminal violations of ERISA. José has defended plan fiduciaries and boards of directors against ERISA litigation alleging breach of fiduciary duty in connection with imprudent investments, excessive fees, and delinquent employee contributions. In addition, he provides guidance to plan sponsors and fiduciaries on meeting their fiduciary responsibilities, plan fees and expenses, and ERISA's prohibited transaction provisions.

José's experience extends to advising his clients in a myriad of labor and employment issues such as: sexual harassment and discrimination charges, retaliation, wrongful termination, restrictive covenants, and traditional labor (grievances, arbitrations, and collective bargaining). José also defends companies against DOL wage and hour investigations. Lastly, he provides interactive harassment training, conducts internal investigations, and drafts employment and severance agreements.

Notably, José began his career as a Federal Investigator with the DOL and was a former complex claims director at a major insurance company.

José is an avid speaker and writer on ERISA and employment law topics. Recent seminars and webinars include: "DOL and IRS Health and Welfare Plan Audits"; "Disability Claims & Procedures"; "Protecting Fiduciaries: Insurance, ERISA Bonding, and More"; "Changes to Valuation of Stock Cases: ESOP Challenges & Enforcement Activity"; "#MeToo in the Workplace and Beyond"; and "Meet the Enforcers from the EEOC, NYS Division of Human Rights, and NYC Commission on Human Rights – A Sexual Harassment Seminar."

Edward Thomas Veal, Senior Counsel, Steptoe & Johnson, LLP

Tom Veal brings more than 40 years of experience to the fields of ERISA, employee benefits, and executive compensation. His principal areas of practice include retirement plan design and drafting, ERISA fiduciary responsibility and prohibited transactions, multiemployer pension plans, Pension Benefit Guaranty Corporation issues, employee stock ownership plans (ESOPs), welfare benefit trusts, and retirement planning for tax-exempt organizations.

Tom is a frequent author in professional publications and periodicals including articles in the New York University Executive Compensation and Employee Benefits Review, Benders Federal Income Taxation of Retirement Plans, Lexis Federal Tax Quarterly, the Journal of Deferred Compensation, the Benefits Law Journal, and the online treatise Lexis Tax Advisor – Federal Topical.

This document from Practical Guidance®, a comprehensive resource providing insight from leading practitioners, is reproduced with the permission of LexisNexis®. Practical Guidance includes coverage of the topics critical to practicing attorneys. For more information or to sign up for a free trial, visit [lexisnexis.com/practical-guidance](https://www.lexisnexis.com/practical-guidance). Reproduction of this material, in any form, is specifically prohibited without written consent from LexisNexis.
