

## **DEPARTMENT OF LABOR**

### **Pension and Welfare Benefits Administration**

#### **[Prohibited Transaction Exemption 93-2;**

Exemption Application Nos. D-8243 and D-8323]

Class Exemption for the Receipt of Certain Services by Individuals for Whose Benefit Individual Retirement Accounts or Retirement Plans for Self-Employed Individuals Have Been Established or Maintained.

AGENCY: Pension and Welfare Benefits Administration, U.S. Department of Labor

ACTION: Grant of class exemption.

SUMMARY: This document contains a final exemption from certain prohibited transaction restrictions of the Internal Revenue Code of 1986 (the Code). The exemption permits the receipt of services at reduced or no cost by an individual for whose benefit an individual retirement account (IRA), or, if self-employed, a Keogh Plan, is established or maintained, or by members of his or her family, from a bank, provided the conditions of the exemption are met. The exemption affects certain individuals with a beneficial interest in the IRAs or Keogh Plans who receive such services, as well as the banks that provide the services.

EFFECTIVE DATE: May 11, 1993.

FOR FURTHER INFORMATION CONTACT: Allison K. Padams, Office of Exemption Determinations, Pension and Welfare Benefits Administration, U.S. Department of Labor, (202) 523-8971 (this is not a toll-free number); or Susan E. Rees, Plan Benefits Security Division, Office of the Solicitor, U.S. Department of Labor, (202) 523-9141 (this is not a toll-free number).

SUPPLEMENTARY INFORMATION: On February 28, 1991, the Department of Labor (the Department) published a notice in the FEDERAL REGISTER (56 FR 8365) of the pendency of a proposed class exemption from the sanctions resulting from the application of sections 4975(a) and (b), 4975(c)(3) and 408(e)(2) of the Code by reason of section 4975(c)(1)(D), (E) and (F) of the Code.<sup>1</sup> The Department proposed the class exemption in response to applications filed on behalf of the American Bankers Association (the ABA) on November 14, 1989 and the Consumer Bankers Association on February 20, 1990. The applications were filed under section 4975(c)(2) of the Code, and in accordance with the procedures set forth in ERISA Procedure 75-1 (40 FR 18471, April 28, 1975).

The notice of pendency gave interested persons an opportunity to comment on the proposal. Twenty-three public comments were received pursuant to the provisions of section 4975(c)(2) of the Code and in accordance with the procedures set forth in ERISA Procedure 75-1. Upon consideration of all the comments received, the Department has determined to grant the proposed class exemption subject to certain modifications. These modifications and the major comments are discussed below.

Discussion of Comments Received

## 1. Scope

The proposed exemption limited relief to transactions involving IRAs and Keogh Plans which are not "employee benefit plans" covered by title I of ERISA.<sup>2</sup> The ABA and a number of other commenters urged the Department to expand the exemption to provide relief for transactions involving simplified employee pensions (SEPs) as defined under section 408(k) of the Code. According to the comments, SEP arrangements are, for all practical purposes, no different than other IRAs covered by the proposed exemption. On the basis of the comments received, the Department has decided that it may be appropriate to provide administrative relief from sections 406(a)(1)(D) and 406(b) of the Employee Retirement Income Security Act of 1974 (ERISA) for transactions involving SEPs.

However, the Department did not propose relief from section 406(b) of ERISA at the time the class exemption was proposed, and pursuant to the requirements of section 408(a) of ERISA, the Department is required to offer interested persons an opportunity to present their views and an opportunity for a hearing before granting an exemption from section 406(b). Therefore, in order not to delay the exemption from section 4975(c)(1)(D), (E) and (F) of the Code for transactions involving IRA and Keogh Plans not covered by title I of ERISA, the Department has decided to grant the exemption described herein, and to simultaneously publish elsewhere in this issue of the FEDERAL REGISTER, a notice of proposed class exemption from sections 406(a)(1)(D) and 406(b) of ERISA for transactions involving the receipt of services at reduced or no cost by a participant covered under a SEP.

Other commenters requested that relief be extended to include all IRAs and Keogh Plans covered by title I of ERISA. As noted above, the extension of relief to all title I IRAs and Keogh Plans is beyond the scope of this proceeding. Moreover, the Department does not agree that, on the basis of current information, an exemption should be proposed to extend relief to IRAs and Keogh Plans covered by title I other than SEPs. Accordingly, the Department has not made the requested modification.

Finally, the ABA urged the Department to modify the final exemption to provide relief from all of section 4975(c)(1) of the Code in order to avoid uncertainty as to the scope and effect of the exemption. The Department is not persuaded that additional relief is necessary for the transactions covered by the exemption. Consequently, the exemption has not been revised in this regard.

## 2. Conditions

Section II(b) of the proposed exemption conditioned relief on the services being of the type which the bank itself could offer consistent with applicable federal and state banking law. Two commenters suggested that the Department modify this condition to permit banks to offer services provided by affiliates of the bank which are not of the type that the bank itself could provide to customers directly (e.g., brokerage services). Other commenters requested that the Department broaden section II(b) to include services provided by third parties. The Department is not persuaded by the commenters that such an expansion of the exemption would be appropriate. The Department, however, recognizes that banks typically contract with third parties to provide customers with products of a de minimis value such as checkbooks which are directly related to the provision of customary banking services. The Department believes that the provision of such incidental products is consistent with the safeguards embodied in the

exemption. To clarify this matter, the final exemption includes a new section III(g) which defines the term "services".

Under section II(c) of the proposed exemption, the services were required to be provided by the bank in the ordinary course of the bank's business to customers who do not qualify for reduced or no cost banking services. Two commenters urged the Department to modify section II(c) to allow banks to offer some services exclusively to relationship banking customers (e.g., consolidated account summaries or special teller lines). The commenters noted that these banking services are part of established and legitimate business practices. The Department finds merit in these comments. However, the Department believes that the limitation on relationship banking services to services that the bank provides to relationship banking customers who do not maintain IRAs or Keogh Plans with the bank is an important safeguard under the exemption. Accordingly, section II(c) has been revised to require that the reduced or no cost banking services must be offered by the bank to customers other than those who qualify for such services by reason of IRAs and Keogh Plans maintained with the bank. In this regard, the Department notes that this condition would preclude the provision of services that specifically relate to the establishment or maintenance of IRAs or Keogh Plans.

Another commenter requested that the final exemption clarify that services provided in the ordinary course of an affiliate's business are also covered by the exemption. The Department wishes to note that relief is available under the exemption for services provided by an affiliate of the bank if such services are of the type that the bank itself could offer consistent with applicable banking law and are offered by the bank on a regular basis to customers who do not maintain IRAs and Keogh Plans with the bank. To the extent that the commenter is requesting additional relief, the Department does not believe that it is appropriate to further revise this condition.

Section II(d) of the proposal required that, for the purpose of determining eligibility to receive services at reduced or no cost, the deposit balance in the IRA or Keogh Plan be treated in the same manner as account balances of the same dollar amount, other than those in IRAs or Keogh Plans, which are maintained by customers of the bank. A number of commenters suggested that this condition was inconsistent with the current practice of the banking industry because the economics of banking require price discrimination by account type. The commenters urged the Department to modify this condition to permit banks to establish different minimum balances for each type of account according to the bank's own rate of return earned on each type of account. The Department recognizes that the exemption as proposed may be inconsistent with the existing practices of some banks, and, therefore, may discourage banks from including IRA and Keogh Plans in their relationship banking programs. However, the Department is concerned that a relationship banking program which establishes a different dollar threshold amount for each type of account in order to qualify for reduced or no cost services could have an adverse impact on IRA and Keogh Plan investments. In light of this concern, but in recognition that many financial institutions do not treat all banking balances as fungible, the Department has determined to revise section II(d) to provide that a relationship banking program would comply with this condition if the deposit balance requirement for IRAs and Keogh Plans is equal to the lowest balance required for any type of account which is counted by the bank in determining eligibility to receive reduced or no cost services. For example, if a bank establishes a relationship banking program under which a customer will be eligible for reduced or no cost services if he maintains a savings account balance of \$1,000 or a Certificate of Deposit (CDs) balance of \$5,000, section II(d) would be satisfied if the minimum balance required for IRAs or Keogh Plans to receive services under this program is \$1,000,

regardless of whether a savings account or CD investment is selected for the IRA or Keogh Plan.

In this regard, the Department notes that relief would not be available under the exemption for programs that determine eligibility on the basis of an aggregate balance of different types of account balances, unless the dollar amount of the IRA or Keogh Plan balance is weighted in the same manner as the dollar amount in the type of account with the lowest minimum balance eligible to participate in the program. For example, section II(d) will not be satisfied if a bank offers a package of services under a program which: (1) requires customers to maintain an aggregate balance of \$10,000 or more; (2) counts only those accounts with a minimum balance of \$1000; and (3) counts, for purposes of aggregation, CDs and checking account balances on a dollar for dollar basis, and passbook accounts, IRAs and Keogh Plans on the basis of 50 cents for each dollar in such accounts. This type of program does not satisfy section II(d) because the IRA and Keogh Plan balances are not weighted in the same manner as the balances of either CDs or checking accounts.

The Department further notes that, under the rule contained in section II(d), if banks offer different packages of services depending on the amount of the customers' balances, the IRA or Keogh Plan customer must be eligible to receive the same services that non-IRA and non-Keogh Plan customers are eligible to receive under the particular relationship banking package. For example, if a bank establishes a multi-level relationship banking program, under which a Level I customer is eligible for reduced or no cost services if he maintains a savings account balance of \$1,000 or a CD balance of \$5,000, the minimum balance required under section II(d) for IRAs or Keogh Plans would be \$1,000, and the IRA or Keogh Plan customer must be eligible to receive the same Level I services as non-IRA and non-Keogh Plan customers. Similarly, if a Level II customer is eligible to receive additional services if he maintains a savings account balance of \$5,000 or a CD balance of \$10,000 the minimum balance required for the IRA or Keogh Plan would be \$5,000, and the IRA or Keogh Plan customer must be eligible to receive the same Level II services as non-IRA and non-Keogh Plan customers.

The Department also notes that relationship banking programs which treat all banking balances as fungible would continue to satisfy section II(d) as revised.

Under section II(e) of the proposal, the receipt of services would have been covered if the rate of return on the IRA or Keogh Plan investment was no less favorable than the rate of return on an identical investment that could have been made at the same time by a customer of the bank who is not eligible for (or who does not receive) reduced or no cost services. Several commenters urged the Department to delete section II(e). Other commenters requested that the Department clarify that section II(e) only requires that the rate of return earned on an IRA or Keogh Plan investment of a relationship banking customer be identical to that of an IRA or Keogh Plan investment of a non-relationship banking customer. In this regard, the Department wishes to note that section II(e) of the proposal was not limited by its terms to a comparison of IRA and Keogh Plan investments by relationship banking customers with IRA and Keogh Plan investments by non-relationship banking customers. The Department believes that a separate condition which requires that identical investments be offered to non-plan customers assures that the IRAs and Keogh Plans are afforded the same investment opportunities which are available to other customers of the bank who do not receive reduced or no cost services. Therefore, the Department cannot conclude that deletion or modification of this section is warranted.

Two commenters requested that the Department substitute the word "similar" for the word "identical" with respect to this condition. Since the adoption of this suggestion would necessitate a subjective determination, the Department does not believe that it would be appropriate to revise section II(e) in this regard.

Two commenters urged the Department to limit section II(e) to those investments made at the same branch of a bank because banks often offer different rates of return at different branches of the bank according to the market conditions of that geographic area. The Department sees merit in these comments and has limited this section to each branch of the bank.

Finally, in response to several comments, the Department notes that section II(e) does not preclude a bank from offering a more favorable rate of return on an IRA or Keogh Plan investment which is otherwise identical to an investment available to other customers of such bank, regardless of participation in the relationship banking program.

### 3. Effective Date

As proposed, the final exemption would be effective as of the date of publication in the FEDERAL REGISTER. The ABA requested that the final exemption provide three types of transitional relief: (1) a delayed effective date of 120 days; (2) the exemption of binding arrangements; and (3) the exemption of binding investments. The ABA stated that banks will need 120 days to make the transition from Announcement 90-1<sup>3</sup> since it contains conditions which are different than those in the proposed exemption. The Department concurs with this comment and believes that a delayed effective date of 120 days is a reasonable period of time for banks to accomplish this transition.<sup>4</sup>

The second type of transitional relief requested is the exemption of binding arrangements involving reduced or no cost services entered into prior to the effective date of the exemption which comply with Announcement 90-1. Lastly, the ABA requested that the Department modify the exemption to permit banks to consider, for relationship banking purposes, binding IRA and Keogh Plan investments made prior to the exemption's effective date that complied with that Announcement. The ABA argued that these arrangements and investments may not meet the conditions of the final exemption, and that banks would be required to disregard them.

The Department is not persuaded by the commenter's argument regarding the provision of additional transitional relief. Under Announcement 90-1, the Service stated that the Announcement would be effective until the Department's final determination regarding the exemption. In this regard, the Department notes that banks were fully aware of the temporary nature of the Announcement, and had the opportunity to develop or alter their relationship banking packages accordingly. In addition, the Department believes that the safeguards contained in the final exemption would be diminished if the exemption were to provide relief for these binding arrangements and investments. Accordingly, the Department believes that a delayed effective date of 120 days adequately addresses the commenter's concerns regarding the need for transitional relief. This effective date provides sufficient time for banks to conform their relationship banking programs and policies to the conditions of the final exemption.

### 4. Definitions

The term bank is defined under the proposal as a bank described in section 408(n) of the Code. One commenter requested that the Department modify the definition of bank to include

institutions which qualify as trustees of IRAs under section 408(a)(2) of the Code. Another commenter urged the Department to include bank affiliates which offer IRAs to customers. In the absence of any showing regarding how the safeguards contained in the exemption would apply to financial institutions described in Code section 408(a)(2) or bank affiliates, the Department is unable to conclude that such modification is warranted.

The proposed exemption defined the term deposit balance as having the same meaning as the term deposits which is contained in section 408(b)(4) of ERISA and defined under 29 CFR 2550.408b-4(c)(3). Thus, deposit balance includes any account upon which a reasonable rate of interest is paid, including a certificate of deposit issued by a bank or similar financial institution. The ABA urged the Department to broaden the definition of deposit balance to encompass all investments made by IRAs and Keogh Plans including those available only to IRAs and Keogh Plans. One of the Department's concerns in developing this exemption was to assure that the rate of return earned on an IRA or Keogh Plan investment is not sacrificed in favor of a customer's receipt of reduced or no cost services. In light of the Department's discussion above regarding the requirement under section II(e) that identical investments be offered to plan and non-plan customers, the Department does not believe that further relief is warranted.

One commenter was concerned about the Department's decision to include brothers, sisters and spouses of brothers or sisters within the definition of "member of his or her family". In this regard, the Department notes that this definition does not preclude a bank from limiting the number of family members entitled to receive relationship banking services under its program. Two other commenters urged the Department to expand this definition to include "domestic partners". The Department has determined not to make this revision because the scope of the term "domestic partners" has not been sufficiently defined.

#### Miscellaneous

1. Two commenters sought clarification from the Department regarding who is eligible to receive relationship banking services under the exemption. In response to the comments the Department has added language to the exemption to clarify that relief is limited under the exemption to the receipt of services by the individual covered under the IRA or Keogh Plan and his or her beneficiaries who are members of the family within the meaning of section III(f) of the final exemption.
2. Two commenters raised the question whether banks can include services which are available to all customers at no cost in their relationship banking programs. The Department notes that the exemption does not preclude banks from offering free services to customers participating in a relationship banking program.
3. A commenter requested that the Department clarify that, for purposes of the exemption, the term "service" includes the provision of life insurance by a credit union to its members. The Department directs the commenter to the Grant of Class Exemption for Certain Transactions Involving Persons for Whose Benefit an Individual Retirement Account or Retirement Plan for Self-Employed Individuals is Established which the Department is also publishing in today's FEDERAL REGISTER.
4. Certain commenters expressed concern whether banks may include credit based products as a method of qualifying for a bank's relationship banking program. In this regard, the Department notes that the preamble to the proposed exemption, in explaining the application of section II(d), contained an example of a relationship

banking program which included loan balances in determining eligibility to receive services at reduced or no cost.<sup>5</sup>

5. In response to one commenter, the Department notes that the exemption does not require banks to include either or both IRAs and Keogh Plans in their relationship banking programs.

## General Information

The attention of interested persons is directed to the following:

(1) In accordance with section 4975(c)(2) of the Code, and based upon the entire record, the Department finds that the exemption is administratively feasible, in the interests of the IRAs and Keogh Plans and of their participants and beneficiaries and protective of the rights of participants and beneficiaries of such plans.

(2) The exemption is supplemental to, and not in derogation of the Code, including statutory or administrative exemptions and transitional rules. Furthermore, the fact that a transaction is subject to an administrative or statutory exemption is not dispositive of whether the transaction is in fact a prohibited transaction.

(3) The exemption is applicable to a transaction only if the conditions specified in the exemption are met.

## Exemption

Accordingly, the following exemption is granted under the authority of section 4975(c)(2) of the Code and in accordance with the procedures set forth in ERISA Procedure 75-1 (40 FR 18471, April 28, 1975).

### Section I: Covered Transaction

Effective May 11, 1993, the sanctions resulting from the application of section 4975 of the Code, including the loss of exemption of an individual retirement account (IRA) pursuant to section 408(e)(2)(A) of the Code, by reason of section 4975(c)(1)(D), (E) and (F) of the Code, shall not apply to the receipt of services at reduced or no cost by an individual for whose benefit an IRA or, if self-employed, a Keogh Plan, is established or maintained, or by members of his or her family, from a bank pursuant to an arrangement in which the deposit balance in the IRA or Keogh Plan is taken into account for purposes of determining eligibility to receive such services, provided that each condition of Section II of this exemption is satisfied.

### Section II: Conditions

(a) The IRA or Keogh Plan, the deposit balance of which is taken into account for purposes of determining eligibility to receive services at reduced or no cost, is established and maintained for the exclusive benefit of the participant covered under the IRA or Keogh Plan, his or her spouse or their beneficiaries.

(b) The services must be of the type that the bank itself could offer consistent with applicable federal and state banking law.

(c) The services are provided by the bank (or an affiliate of the bank) in the ordinary course of the bank's business to customers who qualify for reduced or no cost banking services but do not maintain IRAs or Keogh Plans with the bank.

(d) For the purpose of determining eligibility to receive services at reduced or no cost, the deposit balance required by the bank for the IRA or Keogh Plan is equal to the lowest balance required for any other type of account which the bank includes to determine eligibility to receive reduced or no cost services.

(e) The rate of return on the IRA or Keogh Plan investment is no less favorable than the rate of return on an identical investment that could have been made at the same time at the same branch of the bank by a customer of the bank who is not eligible for (or who does not receive) reduced or no cost services.

### Section III: Definitions

The following definitions apply to this exemption:

(a) The term bank means a bank described in section 408(n) of the Code.

(b) The term IRA means an individual retirement account described in Code section 408(a). For purposes of this exemption, the term IRA shall not include an IRA which is an employee benefit plan covered by title I of ERISA.

(c) The term Keogh Plan means a pension, profit sharing, or stock bonus plan qualified under Code section 401(a) and exempt from taxation under Code section 501(a) under which some or all of the participants are employees described in section 401(c) of the Code. For purposes of this exemption, the term Keogh Plan shall not include a Keogh Plan which is an employee benefit plan covered by title I of ERISA.

(d) The term deposit balance means deposits as that term is defined under 29 CFR 2550.408b-4(c)(3).

(e) An affiliate of a bank includes any person directly or indirectly controlling, controlled by, or under common control with the bank. The term control means the power to exercise a controlling influence over the management or policies of a person other than an individual.

(f) The term members of his or her family refers to beneficiaries of the individual for whose benefit the IRA or Keogh Plan is established or maintained, who would be members of the family as that term is defined in Code section 4975(e)(6), or a brother, a sister, or spouse of a brother or a sister.

(g) The term service includes incidental products of a de minimis value provided by third persons, pursuant to an arrangement with the bank, which are directly related to the provision of banking services covered by the exemption.

Signed at Washington, D.C., this 5th day of January, 1992.



ALAN D. LEBOWITZ  
Deputy Assistant Secretary of Program Operations  
Pension and Welfare Benefits  
Administration

U.S. Department of Labor

<sup>1</sup>Section 102 of Reorganization Plan No. 4 of 1978 (43 FR 47713, October 17, 1978) generally transferred the authority of the Secretary of the Treasury to issue administrative exemptions under section 4975(c)(2) of the Code to the Secretary of Labor.

<sup>2</sup>29 CFR 2510.3-2(d) explains that IRAs described in section 408(a) of the Code will not be considered pension plans subject to title I of ERISA, provided that: (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 without endorsement to permit the sponsor to publicize the program, to collect contributions on behalf of the sponsor through payroll deductions or dues checkoffs and to remit them to the sponsor; 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.

29 CFR 2510.3-3(b) explains that for purposes of title I of ERISA, "employee benefit plan" shall not include a Keogh Plan under which no employees are covered under the plan. In this regard, 29 CFR 2510.3-3(c) states that for purposes of the above referenced section: (1) an individual and his or her spouse shall not be deemed to be employees with respect to a trade or business, whether incorporated or unincorporated, which is wholly owned by the individual and his or her spouse; and (2) a partner in a partnership and his or her spouse shall not be deemed to be employees with respect to the partnership.

<sup>3</sup>The Service issued a nonenforcement policy which provides that the Service will not raise issues concerning the tax effects resulting from possible prohibited transactions arising from certain cash, property or services offered by financial institutions to individuals for whom the financial institution maintains certain IRAs and Keogh Plans. See Announcement 90-1, 1990-2 I.R.B. 31, (January 1, 1990).

<sup>4</sup>In this regard, the Department has consulted with the Service regarding the application of Announcement 90-1. The Service has indicated that the Announcement will continue to be in effect during this 120 day period.

<sup>5</sup>See 56 FR 8367.