

August 2005 / Special Alert

A legal update from Dechert's Employee Benefits and Executive Compensation and Financial Services Groups

## House Committee Approves ERISA Amendments

On June 30, 2005, the House Committee on Education and the Workforce approved the Pension Protection Act of 2005 (H.R. 2830) (the "Bill"), which, if enacted, would make several amendments to the prohibited transaction rules of the Employee Retirement Income Security Act of 1974 ("ERISA"). The Bill also provides a definition of "plan assets" and clarifies certain other ERISA requirements. The highlights of the Bill are described below. The Bill must be approved by the House Ways and Means Committee before it can be acted upon by the full House. Similar legislation is expected to be introduced in the Senate.

### Definition of Plan Asset Vehicle

The Bill would redefine the circumstances under which an entity's assets would be considered "plan assets" for ERISA purposes. In general, the Bill would provide that assets of any entity would not be treated as "plan assets" if, immediately after the most recent acquisition of any equity interest in the entity, less than 50% of the total value of all equity interests in the entity were held by employee benefit plan investors. In addition, an entity would be considered to hold plan assets only to the extent of the percentage of the equity interest owned by benefit plan investors.

The Bill also would modify the definition of "benefit plan investor" to mean only an employee benefit plan subject to ERISA and any plan to which section 4975 of the Internal Revenue Code of 1986 applies; thus, the definition would not include governmental and non-U.S. benefit plans for this purpose. The current plan asset regulation applies a 25% threshold on a class-by-class basis.

### Correction Period for Certain Prohibited Transactions

The Bill would add a new self-correction provision to ERISA. Under the Bill, certain transactions in connection with the acquisition, holding or disposition of any security or commodity, would be exempt from certain prohibited transaction rules (not including the self-dealing rules) if the transaction were corrected before the end of the correction period. The correction period would generally mean the 14-day period beginning on the date on which such fiduciary or party in interest discovers, or reasonably should have discovered, that the transaction would constitute a prohibited transaction. Certain other requirements would apply.

### Definition of Amount Involved

In the case of a prohibited transaction by a party in interest with respect to a plan, the Secretary of Labor may assess a civil penalty against the party in interest of up to 5% of the amount involved. In general, the amount involved means the greater of:

- The amount of money and the fair market value of the other property given
- The amount of money and the fair market value of the other property received

The Bill would add a special rule to the definition of amount involved, such that, in the case of principal transactions involving securities or commodities, the amount involved would include only the amount received by the

disqualified person in excess of the amount such person would have received in an arm's length transaction with an unrelated party.

## **Exemption for Provision of Investment Advice**

Under the Bill, certain transactions related to the provision of investment advice would be exempt from the prohibited transaction rules. These transactions include:

- The provision of advice to a plan, participant or beneficiary
- The sale, acquisition or holding of a security or other property pursuant to the advice
- The direct or indirect receipt of fees or other compensation by the fiduciary adviser in connection with the provision of the advice or in connection with a sale, acquisition, or holding of a security or other property pursuant to the advice

The investment of assets of the plan must be subject to the direction of plan participants or beneficiaries, the advice must be provided to the plan or a participant or beneficiary of the plan by a fiduciary adviser in connection with a sale, acquisition, or holding of a security or other property for purposes of investment of plan assets, and certain other conditions must be satisfied. A fiduciary adviser would generally be a person registered as an investment adviser under the Investment Advisers Act of 1940, a bank or similar financial institution, an insurance company, a broker-dealer registered under the Securities Exchange Act of 1934, or an affiliate or employee of any of the foregoing.

## **Electronic Communication Network Exemption**

Under the Bill, transactions involving the purchase and sale of securities or other property between a plan and a fiduciary or a party in interest would be exempt from the prohibited transaction rules if the transaction were executed through an exchange, electronic communication network, alternative trading system, or similar execution system or trading venue subject to regulation and oversight by the applicable governmental regulating entity, and certain other conditions are met.

## **Foreign Exchange Transaction Exemption**

Under the Bill, foreign exchange transactions between a bank or broker-dealer (or any affiliate of either) and a plan with respect to which the bank or broker-dealer, or any affiliate, is a trustee, custodian, fiduciary or other party in interest would be exempt from the prohibited transaction rules if the transaction were in connection with the purchase or sale of securities, the bank or broker-dealer (or any affiliate) did not have investment discretion or provide investment advice with respect to the securities transaction, and certain other conditions were met. This proposal would expand on the prohibited transaction class exemptions covering certain foreign exchange transactions that the Department of Labor previously issued in 1994 and 1998.

## **Block Trading Exemption**

Under the Bill, transactions involving the purchase or sale of securities between a plan and a party in interest (other than a fiduciary) would be exempt from the prohibited transaction rules if the transaction were a block trade (i.e., any trade which will be allocated across two or more client accounts of a fiduciary). Certain conditions would apply, including that at the time of the transaction, the interest of the plan may not exceed 10% of the aggregate size of the block trade.

## **Exemption for Provision of Services**

Under the Bill, certain transactions between a plan and a party that is a party in interest solely by reason of providing services would be exempt from the prohibited transaction rules, but only if in connection with such transaction the plan receives no less, nor pays no more, than adequate consideration. Adequate consideration, in the case of a security for which there is a generally recognized market, would be defined to mean the price prevailing on a national securities exchange, taking into account factors such as the size of the transaction and marketability of the security.

If the security is not traded on a national securities exchange, adequate consideration would be defined to mean a price not less favorable to the plan than the offering price for the security as established by the current bid and asked prices quoted by persons independent of the issuer and of the party in interest, taking into account factors such as the size of the transaction and marketability of the security.

## Bonding

ERISA requires every fiduciary of an employee benefit plan and every person who handles funds or other property of a plan to be bonded. The Bill would exempt from the ERISA bonding requirement broker dealers that are subject to Section 15 of the Securities Exchange Act of 1934 and entities registered under the Investment Advisers Act of 1940. ERISA currently provides an exemption from the bonding requirement only for corporations that are authorized to exercise trust powers or to conduct an insurance business, and that satisfy certain capitalization requirements.

## IRS Circular 230 Disclosure

To ensure compliance with requirements imposed by the IRS, we inform you that any U.S. federal tax advice contained in this communication (including any attachments) is not intended or written to be used, and cannot be used, for the purpose of (a) avoiding penalties under the Internal Revenue Code, or (b) promoting, marketing or recommending to another party any transaction or matter addressed herein.



This legal update was authored by Susan M. Camillo (+1.617.728.7125; [susan.camillo@dechert.com](mailto:susan.camillo@dechert.com)) and Kathleen Ziga (+1.215.994.2674; [kathleen.ziga@dechert.com](mailto:kathleen.ziga@dechert.com)).

## Practice group contacts

For further information contact the authors, one of the attorneys listed or any Dechert LLP attorney with whom you are in regular contact. Visit us at [www.dechert.com/employeefenefits](http://www.dechert.com/employeefenefits) or [www.dechert.com/financialservices](http://www.dechert.com/financialservices).

### **Sander M. Bieber**

Washington  
+1.202.261.3308  
[sander.bieber@dechert.com](mailto:sander.bieber@dechert.com)

### **Susan M. Camillo**

Boston  
+1.617.728.7125  
[susan.camillo@dechert.com](mailto:susan.camillo@dechert.com)

### **Douglas P. Dick**

Newport Beach  
+1.949.442.6060  
[douglas.dick@dechert.com](mailto:douglas.dick@dechert.com)

### **Ruth S. Epstein**

Washington  
+1.202.261.3322  
[ruth.epstein@dechert.com](mailto:ruth.epstein@dechert.com)

### **Susan C. Ervin**

Washington  
+1.202.261.3325  
[susan.ervin@dechert.com](mailto:susan.ervin@dechert.com)

### **Joseph R. Fleming**

Boston  
+1.617.728.7161  
[joseph.fleming@dechert.com](mailto:joseph.fleming@dechert.com)

### **Brendan C. Fox**

Washington  
+1.202.261.3381  
[brendan.fox@dechert.com](mailto:brendan.fox@dechert.com)

### **David J. Harris**

Washington  
+1.202.261.3385  
[david.harris@dechert.com](mailto:david.harris@dechert.com)

### **Robert W. Helm**

Washington  
+1.202.261.3356  
[robert.helm@dechert.com](mailto:robert.helm@dechert.com)

### **Jane A. Kanter**

Washington  
+1.202.261.3302  
[jane.kanter@dechert.com](mailto:jane.kanter@dechert.com)

### **Stuart Kaswell**

Washington  
+1.202.261.3314  
[stuart.kaswell@dechert.com](mailto:stuart.kaswell@dechert.com)

### **George J. Mazin**

New York  
+1.212.698.3570  
[george.mazin@dechert.com](mailto:george.mazin@dechert.com)

### **Jack W. Murphy**

Washington  
+1.202.261.3303  
[jack.murphy@dechert.com](mailto:jack.murphy@dechert.com)

### **John V. O' Hanlon**

Boston  
+1.617.728.7111  
[john.ohanlon@dechert.com](mailto:john.ohanlon@dechert.com)

### **Jeffrey S. Puretz**

Washington  
+1.202.261.3358  
[Jeffrey.puretz@dechert.com](mailto:Jeffrey.puretz@dechert.com)

### **Jon S. Rand**

New York  
+1.212.698.3634  
[jon.rand@dechert.com](mailto:jon.rand@dechert.com)

### **Keith T. Robinson**

Washington  
+1.202.261.3386  
[keith.robinson@dechert.com](mailto:keith.robinson@dechert.com)

### **Frederick H. Sherley**

Charlotte  
+1.704.339.3100  
[frederick.sherley@dechert.com](mailto:frederick.sherley@dechert.com)

### **Patrick W.D. Turley**

Washington  
+1.202.261.3364  
[patrick.turley@dechert.com](mailto:patrick.turley@dechert.com)

### **David A. Vaughan**

Washington  
+1.202.261.3355  
[david.vaughan@dechert.com](mailto:david.vaughan@dechert.com)

### **Brian S. Vargo**

Philadelphia  
+1.215.994.2880  
[brian.vargo@dechert.com](mailto:brian.vargo@dechert.com)

### **Kathleen Ziga**

Philadelphia  
+1.215.994.2674  
[kathleen.ziga@dechert.com](mailto:kathleen.ziga@dechert.com)

**U.S.**

Boston  
Charlotte  
Harrisburg  
Hartford  
New York  
Newport Beach

**U.K./Europe**

Brussels  
Frankfurt  
London  
Luxembourg  
Munich  
Paris

© 2005 Dechert LLP. All rights reserved. Materials have been abridged from laws, court decisions, and administrative rulings and should not be considered as legal opinions on specific facts or as a substitute for legal counsel.