P/OPINION 75-108

March 5, 1975

Dear :

This letter is in response to your letter of February 8, 1975, requesting clarification concerning loans from a pension plan to employees of the employer who established the pension plan.

Section 414(c)(1) of the Employee Retirement Income Security Act of 1974 governs all such plans pursuant to a contract which was in effect on July 1, 1974, and if such loans meet the three tests set forth in such section, they are not considered to be a prohibited transaction until June 30, 1984.

With respect to all loans entered into subsequent to the effective date of the Act and which were not pursuant to a contract which was in effect on July 1, 1974, such loans would be prohibited under section 406 of the Act, unless they met the statutory exemption set forth in section 408(b)(1) of the Act.

The Joint Explanatory Statement of the Conference Committee, in explaining the basis for the statutory exemption, states as follows:

> "To be permitted, such loans must be made in accord with specific provisions in the plan governing such loans. In addition, a reasonable interest rate must be charged and the loan must be adequately secured. Such loans must be made available to all participants on a reasonably equivalent basis. Consequently, the plan could not unreasonably discriminate between applicants on the basis of, e.g., age, or sex; but the plan could make distinctions on the basis of, e.g., credit worthiness or financial need. Also, such loans cannot be made available to highly-compensated employees in an amount greater than the amount available to other employees. The conferees intend that this will allow a plan to lend the same percentage of a person's vested benefits to participants

> with both large and small amounts of accrued vested benefits. (However, the percentage is to be consistent with the requirements of adequate security). The conferees also intend that a plan may provide that the same dollar amounts may be loaned to participants and beneficiaries without regard to the amount of their vested benefits if adequate security is otherwise provided. For example, a plan could provide for loans to participants and beneficiaries in an amount up to, e.g., $30,000 to buy a house (even if the $30,000 is greater than the amount of the participant's or beneficiary's vested benefits) if the loan is adequately secured by, e.g., a first mortgage on the house."

If any new loans from the plan to employees are proposed, they would be prohibited unless they fall within the exemption provided by section 408(b)(1) as elucidated by the Conference Report.

Sincerely,