ERISA OPINION

U.S DEPARTMENT OF LABOR
Pension and Welfare Benefit Programs
Washington, D.C. 20216

**MAR 21 1977**

Homer L. Elliott, Esquire
Steptoe and Johnson
1250 Connecticut Avenue, N.W.
Washington, D. C. 20036

Dear Mr. Elliott:

This is in reply to your letter concerning the provisions of the Employee Retirement Income Security Act of 1974 (ERISA). I regret that our heavy workload has resulted in a delay in responding to your letter.

Specifically you request opinions that (l) the proposed sales by Mr. Robert J. Pond and Mrs. Barbara Pond Allen of class B common stock of Advance Machine Company (AMC) to the AMC Employee Stock Ownership Trust (the Trust) will not constitute transactions described in ERISA section 406 by reason of the application of ERISA section 408(e), provided that the Trust acquires the stock for "adequate consideration" and (2) in determining whether "adequate consideration" has been paid, the shareholders and trustee may rely in good faith on an appraisal of the fair market value of the stock by a reputable, independent, outside organization as establishing adequate consideration to be paid.

You state the following facts. It is proposed that Mr. R. J. Pond and Mrs. B. P. Allen will sell to the Trust, for cash, approximately 15,000 shares and 5,000 shares, respectively, of $.50 par value class B nonvoting common stock. There is no trading in this stock. The above named shareholders are directors of AMC, and Mr. R. J. Pond is also the president of AMC. All shares to be sold to the Trust will be sold at a price not in excess of their fair market value on the date of transfer as determined through appraisal. The appraisal will be conducted by a reputable, independent, outside organization. There will be no commission charged with respect to any sale. It is also anticipated that in future years AMC shareholders, who may or may not be parties in interest with respect to the Trust, will sell additional shares of AMC common stock to the Trust for cash and/or notes. Section 6 of the AMC Employee Stock Ownership Plan (the Plan) permits the Trust to acquire AMC stock from AMC or its shareholders with funds contributed by AMC or borrowed by the Trust.

A copy of a letter from the Internal Revenue Service (the Service) which you submitted to this office shows that the Service has determined that the Plan, established December 18, 1974, will qualify under section 401(a) of the Internal Revenue Code of 1954 if the proposed amendments submitted to the Service by letter dated February 4, 1976, are adopted. However, you believe that the Plan has at all times been a qualified plan under section 401(a) of the Code. You also believe that the Plan is an eligible individual account plan under section 407(d)(3) of ERISA because it is an individual account plan under section 3(34) and is a stock bonus plan or employee stock ownership plan. No copies of the Plan or of the proposed sales agreement have been submitted to this office.

Under section 3(14)(H) of ERISA, an employee, officer, director (or an individual having powers or responsibilities similar to those of officers or directors), or a ten per cent or more shareholder directly or indirectly, of an employer any of whose employees are covered by an employee benefit plan is a party in interest with respect to such plan. As Mr. R. J. Pond and Mrs. B. P. Allen are directors of AMC, some of whose employees are covered by the Plan, we agree with your conclusion that Mr. R. J. Pond and Mrs. B. P. Allen are parties in interest with respect to the Plan.

Section 406(a)(1)(A) of ERISA prohibits a fiduciary with respect to a plan from causing the plan to engage in a transaction, if he knows or should know that such transaction constitutes a direct or indirect sale or exchange, or leasing, of any property between the plan and a party in interest. However, section 408(e) provides that sections 406 and 407 shall not apply to the acquisition or sale by a plan of qualifying employer securities (as defined in section 407(d)(5)) or acquisition, sale or lease by a plan of qualifying employer real property (as defined in section 407(d)(4)) (1) if such acquisition, sale, or lease is for adequate consideration (with a special rule in the case of a marketable obligation, not applicable to this case), (2) if no commission is charged with respect thereto, and (3) if (A) the plan is an eligible individual account plan (as defined in section 407(d)(3)) or (B) in the case of an acquisition or lease of qualifying employer real property by a plan which is not an eligible individual account plan, or of an acquisition of qualifying employer securities by such a plan, the lease or acquisition is not prohibited by section 407(a) (relating to the ten per cent limitation with respect to acquisition and holding of employer securities and employer real property by certain plans).

Common stock issued by an employer of employees covered by an employee benefit plan constitutes qualifying employer securities within the meaning of section 407(d)(5) of ERISA. Under section 3(18)(B), the term "adequate consideration," for purposes of the above-mentioned ERISA sections, means, in the case of an asset other than a security for which there is a generally recognized market, the fair market value of the asset as determined in good faith by the trustee or named fiduciary pursuant to the terms of the plan and in accordance with regulations promulgated by the Secretary of Labor. Such regulations have not yet been issued.

Section 407(d)(3) classifies stock bonus plans and employee stock ownership plans, among others, as eligible individual account plans if they are individual account plans. The term "individual account plan" is defined by section 3(34) as a pension plan which provides for an individual account for each participant and for benefits based solely upon the amount contributed to the participant's account, and any income, expenses, gains, and losses, and any forfeitures of accounts of other participants which may be allocated to such participant's account. The term "employee stock ownership plan" is defined by section 407(d)(6) as an individual account plan (A) which is a stock bonus plan which is qualified, or a stock bonus plan and money purchase plan both of which are qualified, under section 401 of the Code, and which is designed to invest primarily in qualifying employer securities and (B) which meets such other requirements as the Secretary of the Treasury may prescribe by regulation. Proposed regulations under section 407(d)(6) were published on July 30, 1976 (copy enclosed), but have not yet been finalized.

Based upon the foregoing, we conclude that the proposed sales by Mr. R. J. Pond and Mrs. B. P. Allen to the Plan will meet the requirements of section 408(e) of ERISA if the Plan is an eligible individual account plan within the meaning of section 407(d)(3) or if the acquisition is not prohibited by section 407(a), and if the Trust acquires the stock for adequate consideration within the meaning of section 3(18).

Pursuant to section 5.02(a) of the Department's Advisory Opinion Procedure (ERISA Procedure 76-1, copy enclosed) the Department ordinarily will not issue advisory opinions with respect to, among other things, section 3(18) of ERISA relating to whether certain consideration constitutes adequate consideration.

Accordingly, we cannot issue an opinion on the second issue stated above. In the absence of regulations under section 3(18), determination as to adequate consideration must be made on a case by case basis by the plan trustees or other appropriate named fiduciaries in light of all relevant facts and circumstances.

In addition, no opinion is provided as to whether the proposed sale is consistent with the fiduciary requirements of section 404(a)(1) of ERISA.

Sincerely,

Fred W. Stuckwisch
Director
Office of Regulatory
Standards and Exceptions

Enclosures