

RETIREMENT PLAN LOANS WILL BE EXEMPT FROM TRUTH IN LENDING RULES UNDER THE NEW REGULATION Z

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When the Truth in Lending Act ("TILA") was enacted, it's intention was twofold: 1) to provide meaningful disclosures so consumers would be able to compare available credit terms and minimize uninformed use of credit; and 2) to protect consumers against inaccurate and unfair credit billing and credit card practices. The provisions of TILA extend to participant loans issued by a retirement plan in certain circumstances under Regulation Z, as explained below. The Board of Governors of the Federal Reserve (the "Board") recently amended Regulation Z to improve the disclosures that creditors provide to consumers. This newly amended rule contains a specific exemption for employer-sponsored retirement plan loans. The effective date of the revised regulation is July 1, 2010

<http://edocket.access.gpo.gov/2009/pdf/E8-31185.pdf>.

Current Law

Current TILA requires retirement plans to disclose specific financial information if the plan issues more than twenty five (25) loans not secured by a dwelling, or more than five (5) loans secured by a dwelling. The information to be disclosed includes: the amount financed, the finance charge, the annual percentage rate, procedures for repayment, etc. The 25/5 loan issuance is the standard to be used to determine if a plan is considered to be extending consumer credit

and, therefore, subject to Regulation Z. The applicable time frame to determine the number of loans issued is the current calendar year or the preceding calendar year.

Retirement Plan Exemption

The revised regulation (Section 226.3(g)) exempts employer-sponsored retirement plan loans from the above requirements. More specifically, an extension of credit in an employer-sponsored retirement plan qualified under Internal Revenue Code ("Code") Section 401(a), a tax-sheltered annuity under Code Section 403(b), or eligible governmental deferred compensation plan under Code Section 457(b) will no longer be subject to the disclosure rules as of the effective date of the new rule (July 1, 2010). In order for the exemption to apply, however, the plan-issued loan must be in compliance with the Code and be issued from vested funds.

The exemption will apply regardless of whether the plan is subject to ERISA, and regardless of the number of loans. However, loans issued for amounts in excess of a participant's vested account balance (i.e., plans that allow loans up to a certain dollar amount not to exceed \$10,000 regardless of a participant's vested balance), or that violate the Code, will continue to be subject to the disclosures requirements contained in the amended Regulation Z.

The Board lists several reasons for implementing the exemption. Mainly, the interest and principal of plan loans are reinvested into the participant's account without involvement of a third party creditor imposing finance charges on the participant, and the cost associated with plan loans are typically less than the costs of third party loans. Additionally, administrative fee disclosures will still be required under Department of Labor regulations.

Notwithstanding the Board's reasoning and the general exemption, it should be noted that plans issuing credit cards will not be exempt and will still be subject to some of the requirements of Regulation Z (Section 226.12 (a) and (b)). Strict application guidelines must be followed and the plan must limit the card holder liability for unauthorized use to the lesser of the amount obtained by the unauthorized use or \$50. The requirements of this Section appear to have been (and will continue to be) a deterrent for plans considering a credit card loan feature.

Delayed Effective Date

In order to allow financial institutions enough time to update their forms and disclosure materials, total compliance is not required before July 1, 2010. The retirement plan exemption is not effective prior to that date. Although there is a transition period, during which the language of the disclosures need only partially comply with the new rules, there is no mention of early reliance. Therefore, without future guidance on earlier reliance of the exemption, plans presently subject to Regulation Z in its current form must continue to provide the required disclosures.



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