

U.S. Department of Labor

Labor-Management Services Administration
Washington, D.C. 20216



Reply to the Attention of:

Neil Grossman
(202) 523-6915

MAR 23 1981

Reeves C. Westbrook, Esq.
Covington & Burling
888 Sixteenth Street, N.W.
Washington, D.C. 20006

Re: Consumers United Group, Inc.
Identification No. F-1539A

Dear Mr. Westbrook:

This is in reply to your letters of May 5, 1980 and July 10, 1980, requesting an advisory opinion that certain proposed transactions involving the Consumers United Group, Inc. Profit Sharing Plan (the Plan) are exempt from the prohibited transaction provisions of section 406 of the Employee Retirement Income Security Act of 1974 (ERISA) by virtue of section 408(e) of ERISA.

Your letters contain the facts and representations set forth below:

Consumers United Group, Inc. (CUG), a Delaware corporation, was formed in 1969 to hold the stock of various foreign and domestic subsidiaries involved, among other things, in underwriting life and health insurance, in serving as insurance brokers, agents and administrators, in providing basic computer system software and services, and in marketing "self-appraisal" questionnaires.

The Plan was adopted in 1973 by CUG and its domestic subsidiaries. Under its terms, contributions may be made, at the discretion of CUG's directors, out of the current net income before taxes or the accumulated earned surplus of CUG and its subsidiaries. Contributions are allocated to separate accounts maintained for each member in accordance with the number of calendar quarters the member participated in the Plan during the taxable year for which the contribution was made. Income is allocated on the basis of the size of members' accounts. Benefits are paid upon termination of employment, either over ten years or in a lump sum, or are paid in the form of an annuity or a joint and survivor annuity commencing after age 55 and before age 70.

The National Savings and Trust Company, a party unrelated to CUG, acts as trustee of the Plan. Trust instruments provide that the trustee may, and CUG desires the Plan to, invest all of its funds in the capital stock of CUG.

In 1974, the Plan purchased 250 shares of Class A Common Stock from CUG in exchange for \$191,702.49 in cash and the Plan's note in the amount of \$1,519,297.51. This stock constitutes the sole significant asset of the Plan.

CUG now proposes to reorganize for a number of reasons, including the facts that the Plan has experienced difficulty meeting the cash-flow requirements for benefit payments and that the stock has no market and has paid no dividends. As part of the reorganization, CUG will create a new class of stock, interest-bearing Cumulative Preferred Stock. Alex. Brown & Sons, an independent investment banker, will, at CUG's expense, determine the number of shares of Preferred Stock equal in fair market value to the fair market value of the shares of Common Stock held by the Plan less the fair market value of the Plan's note to CUG. If the trustee is satisfied with the appraisal, the Plan will exchange its Common Stock for the number of shares of Preferred Stock equivalent in fair market value to the Common Stock minus the note. The note and the Common Stock involved in the exchange will be cancelled.

CUG will then purchase the Preferred Stock from the Plan in installments on fifteen annual settlement dates. The fair market value per share of preferred stock will be determined, at each settlement date, by Alex. Brown & Sons or another comparable investment banking advisor acceptable to both the trustee and CUG. CUG will pay each appraisal fee. No commissions will be paid in connection with the proposed transactions.

For purposes of this opinion, you ask us to assume the adequacy of consideration in the proposed transactions. Given this assumption, you request our opinion that

- (1) the Plan's exchange of Common Stock for Preferred Stock and the cancellation of the note does not constitute a prohibited transaction under section 406 of ERISA and
- (2) the purchase of the Preferred Stock from the Plan by CUG, under the circumstances described above, does not constitute a prohibited transaction under section 406 of ERISA.

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 a plan and a party in interest.

Section 3(14)(C) of ERISA defines the term "party in interest" as an employer any of whose employees are covered by an employee benefit plan. CUG is a party in interest with respect to the Plan because it is an employer of employees covered by the Plan. Thus, absent a statutory or administrative exemption, the exchange of the Common Stock for the Preferred Stock and the

cancellation of the note, on the one hand, and each purchase by CUG of Preferred Stock from the Plan, on the other, would constitute a prohibited transaction within the meaning of section 406(a)(1)(A) of ERISA.

Section 408(e) of ERISA, however, provides, in pertinent part, that section 406 and 407 of ERISA do not apply to the acquisition or sale by a plan of qualifying employer securities (as defined in section 407(e)(5)), if the following three conditions are satisfied:

- (1) the acquisition or sale is for adequate consideration,
- (2) no commission is charged with respect to the acquisition or sale, and
- (3) the plan is an eligible individual account plan (as defined in section 407(d)(3)).

Section 3(34) of ERISA defines an "individual account plan" 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. Based on the facts and representations contained in your letters of May 5, 1980 and July 10, 1980, it is the opinion of the Department of Labor (the Department) that the Plan is an "individual account plan" within the meaning of section 3(34) of ERISA.

Section 407(d)(3) of ERISA defines an "eligible individual account plan" to include an individual account plan which is a profit-sharing, stock bonus, thrift, or savings plan, and which explicitly provides for the acquisition and holding of qualifying employer securities.

Section 407(d)(1) of ERISA, in pertinent part, defines the term "employer security" to mean a security issued by an employer of employees covered by the plan. Under section 3(20) of ERISA, a "security" has the same meaning as such term has under section 2(1) of the Securities Act of 1933. Since CUG is an employer of employees covered by the Plan, and the shares of CUG Common Stock and Preferred Stock are securities, as defined in section 2(1) of the Securities Act of 1933, such shares are "employer securities" within the meaning of section 407(d)(1) of ERISA.

Section 407(d)(5) of ERISA defines the term "qualifying employer security" to mean an employer security which is stock or a marketable obligation. To date, the Department has taken no position on the issue of what securities constitute "stock" for purposes of section 407(d)(5). We note, however, that, regardless of the label applied to a security, the Department expects any security which is in the nature of debt to comply with the definition of "marketable obligation" set forth in section 407(e) of ERISA in order to be considered a "qualifying employer security."

Based on the facts and representations contained in your letters of May 5, 1980 and July 10, 1980, the Department has determined that the Plan is an individual account plan which is a

profit-sharing plan, that the Plan explicitly provides for the acquisition and holding of qualifying employer securities, e.g., the capital stock of CUG, and that the Plan is, accordingly, an "eligible individual account plan" within the meaning of section 407(d)(3) of ERISA.

Assuming, per your request, that consideration in the proposed transactions is adequate, and based on your representation that no commissions will be charged and on our determination that the Plan is an "eligible individual account plan," and provided that the CUG Preferred Stock constitutes "stock" or a "marketable obligation" within the meaning of section 407(d)(5) of ERISA, it is the Department's opinion that the relief provided in section 408(e) of ERISA will apply to

- (1) the Plan's surrender of its Common Stock to CUG in exchange for Preferred Stock and the cancellation of the Plan's note held by CUG, and
- (2) each purchase by CUG of Preferred Stock from the Plan.

Our consideration of the proposed transactions does not relate to any provisions of ERISA not discussed in this letter. Thus, for example, we are not rendering any opinion as to whether the proposed transactions, or the Plan's continued holding of the Common Stock from 1974 until the completion of the proposed transactions, are consistent with the general fiduciary responsibility provisions of section 404 of ERISA.

We also render no opinion as to whether the extension of credit by CUG to the Plan in connection with the Plan's initial purchase of the Common Stock is covered by the transitional rule contained in section 414(c)(1) of ERISA. We note, however, that, if not covered by section 414(c)(1), the extension of credit would, as of January 1, 1975, constitute a prohibited transaction, the "correction" of which would fall within the jurisdiction of the Internal Revenue Service (the Service). The "correction" required by the Service could conceivably affect the ability of the parties to carry out the proposed transactions in the manner set forth in your letters.

Under Reorganization Plan No. 4 of 1978 (Executive Order 12108, 44 FR 1065), effective December 31, 1978, the authority of the Secretary of the Treasury to issue rulings under section 4975 of the Internal Revenue Code of 1954 (the Code) has been transferred, with certain exceptions not here relevant, to the Secretary of Labor, and the Secretary of the Treasury shall be bound by the rulings issued by the Secretary of Labor pursuant to such authority. Accordingly, it is the Department's position that the opinion set forth herein applies, to the extent relevant, to section 4975 of the Code.

This letter is an advisory opinion under ERISA Procedure 76-1. Accordingly, it is issued subject to the provisions of that procedure, including section 10 thereof (relating to the effect of advisory opinions).

Sincerely,

Alan D. Lebowitz
Assistant Administrator for Fiduciary Standards
Pension and Welfare Benefit Programs