U.S. Department of Labor

Pension and Welfare Benefits Administration
Washington, D.C. 20210

December 9, 1994

94-42A
ERISA SECTION
407(d)(3) and (9)

Ms. Carol H. Jewett
Vinson & Elkins
2300 First City Tower
1001 Fannin
Houston, Texas 77002-6760

Dear Ms. Jewett:

This is in response to your request on behalf of the Enron Corporation and certain of its subsidiaries (Enron) for an advisory opinion concerning the application of Title I of the Employee Retirement Income Security Act of 1974 (ERISA) to a grandfathered floor-offset arrangement under section 9345(a)(3) of the Omnibus Budget Reconciliation Act of 1987 (OBRA 1987). Specifically, you inquire whether certain plan amendments which Enron proposes to adopt in terminating the floor-offset arrangement over a period of five years would cause the arrangement to lose its grandfathered status.

You state that Enron established the floor-offset arrangement before December 18, 1987, and has maintained it continuously since its establishment. The floor-offset arrangement consists of the Enron Corporation Retirement Plan (the Retirement Plan), a defined benefit plan, and the Enron Corporation Employee Stock Ownership Plan (the ESOP), a leveraged stock bonus plan designed to invest primarily in Enron stock. Under the arrangement, the annuity values of a portion of individual participants' accounts (the Offset Accounts) in the ESOP as of certain determination dates serve as offsets with respect to benefits accrued after December 31, 1986, under the Retirement Plan.[1]

You further represent that Enron proposes to amend the plans in order to terminate the floor offset arrangement over a five year period, and thereafter to continue the ESOP and the Retirement Plan as ongoing, independent plans. Enron also proposes to convert the current Retirement Plan benefit formula to a new, cash balance benefit formula.[2] Accruals under the new benefit formula would begin January 1, 1996. The offsets, however, would apply only with regard to accruals under the current benefit formula from January 1, 1987 to December 31, 1994; they would not affect accruals under the new cash balance formula.

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[1] The value of the ESOP offset is based on the amount of a monthly single life annuity that could be purchased by the value of an individual's ESOP Offset Account as of certain determination dates (generally the date of commencement of Retirement Plan benefit payments or, if earlier, the date(s) of distribution(s) from the Offset Account).

[2] You indicate that the cash balance formula adversely affects certain participants who have attained the age of fifty and completed five years of service under the Retirement Plan as of January 1, 1995, and who thereafter retire from employment with Enron at any time within the next seven years. Enron will amend the Retirement Plan to provide that such individuals accrued benefits on and after January 1, 1995, will be equal to the greater of (1) the amended and restated Retirement Plan's cash balance formula increased by certain allocations to the ESOP or (2) the Retirement Plan's benefit formula in effect on December 31, 1994.

With respect to the ESOP, you represent that no additional shares of Enron stock would be allocated to participants' Offset Accounts after December 31, 1994,[3] and that their Offset Accounts would become 100% vested as of that date. Each January 1st over the five-year period from 1996-2000, the value of one-fifth of the shares of Enron stock credited to each participant's Offset Account would be computed, permanently fixing that component of the offset. You indicate that Enron has proposed a gradual, five-year phase-out schedule to avoid market distortions in the trading of Enron stock, to reduce the risk of fixing the offsets based on an aberrant value, and to deter participants from making precipitous decisions regarding the disposition of amounts that become distributable from their Offset Accounts. At the time that the value of each component is fixed, and periodically thereafter, ESOP participants would be given the right to withdraw the fixed portion of their Offset Accounts, to leave it in the ESOP, or to roll it over either to an individual retirement account or to the Enron Corporation Savings Plan, a defined contribution plan which provides participants with a number of investment alternatives.

In effect, you have requested an advisory opinion that: (1) the cessation of accruals under the current Retirement Plan formula and the conversion of the ESOP offsets to fixed amounts, as described above, would not cause the grandfather provision in section 9345(a)(3) of OBRA 1987 to be inapplicable to the floor-offset arrangement during the five-year period that the arrangement is being terminated; and (2) once all offsets have been computed and converted to fixed amounts, the ESOP will not be subject to the floor-offset provisions in section 407(d) of ERISA.

Section 406(a)(1)(E) 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 acquisition on behalf of the plan of any employer security or employer real property in violation of section 407(a). Section 406(a)(2) of ERISA provides that no fiduciary who has authority or discretion to control or manage the assets of a plan shall permit the plan to hold any employer security or employer real property if he or she knows or should know that the holding of such security or real property violates section 407(a).

Section 407(a) provides, in part, that (1) a plan may not acquire or hold any employer security which is not a qualifying employer security, and (2) a plan may not acquire any qualifying employer security if immediately after such acquisition the aggregate fair market value of employer securities and employer real property held by the plan exceeds 10 percent of the fair market value of the assets of the plan. Section 407(b)(1) of ERISA, however, provides in part that the 10 percent limitation of section 407(a) shall not apply to the acquisition or holding of qualifying employer securities by an eligible individual account plan.

Section 407(d)(3)(A) of ERISA defines "eligible individual account plan" to include an individual account plan which is (i) a profit-sharing, stock bonus, thrift or savings plan, (ii) an employee stock ownership plan, or (iii) a money purchase plan which was in existence on the date of enactment of ERISA and which on such date invested primarily in qualifying employer securities. Such term excludes an individual retirement account or annuity described in section 408 of the Internal Revenue Code. Section 407(d)(3)(B) provides that notwithstanding subparagraph (A), a plan shall be treated as an eligible individual account plan with respect to the acquisition or holding of qualifying employer real property or qualifying employer securities only if such plan explicitly provides for acquisition and holding of qualifying employer securities or qualifying employer real property (as the case may be). Section 407(d)(3)(C) of ERISA, as added by section 9345(a)(1) of OBRA 1987, provides that the term "eligible individual account plan" does not include any individual account plan the benefits of which are taken into account in determining the benefits payable to a participant under any defined benefit plan.

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[3] You represent that the last allocations to participants' Offset Accounts occurred as of December 31, 1993. Although no additional shares may be allocated to participants' Offset Accounts, dividends on shares of Enron Stock in the Offset Accounts would continue to be credited to such accounts and invested in Enron Stock.

Section 407(d)(9) of ERISA, as added by section 9345(a)(2) of OBRA 1987, provides that for purposes of section 407, an arrangement which consists of a defined benefit plan and an individual account plan shall be treated as one plan if the benefits of such individual account plan are taken into account in determining the benefits payable under such defined benefit plan.

Section 9345(a)(3) of OBRA 1987 provides that sections 407(d)(3)(C) and 407(d)(9) shall apply with respect to arrangements established after December 17, 1987. Thus, sections 407(d)(3)(C) and 407(d)(9) of ERISA do not apply to floor offset arrangements established on or before December 17, 1987.

On the basis of the facts and representations contained in your submissions, it is the opinion of the Department that the amendment of the plans to progressively terminate the floor-offset arrangement over a five year period would not render the grandfather provision contained in section 9345(a)(3) of OBRA 1987 inapplicable during the period that the arrangement is being terminated.[4]

With regard to your second question, it is the opinion of the Department that, under the circumstances described, the ESOP would not be subject to sections 407(d)(3) and (9) of ERISA after all remaining offsets under the terminating floor-offset arrangement have been finally computed and fixed.

This letter deals only with issues arising under section 407(d)(3) and (9) of ERISA; the Department has not considered the effect of any other provision of ERISA or the Internal Revenue Code as they may relate to your request.[5] This letter is an advisory opinion under ERISA Procedure 76-1 (41 Fed. Reg. 36282, Aug. 27, 1976). Section 10 of the Procedure explains the effect of an advisory opinion.

Sincerely,

ROBERT J. DOYLE
Director of Regulations and Interpretations

[4] As you represent, the material changes to the Retirement Plan are in the nature of benefit formula changes for future accrual purposes and to phase out the offset arrangement over a five-year period. At the end of the phase out of the offset, no benefit under the Retirement Plan, as amended, will be offset by any accounts or allocations under the ESOP, with the possible exception of those participants described in footnote two above. Such participants, whom you have identified as potentially adversely affected by these amendments, will receive benefits based on the greater of the pre- or post-amendment benefit formula.

[5] Specifically, no opinion is expressed regarding the ESOP requirements imposed by ERISA and the applicable regulations, or the requirement in section 204(h)(1) of ERISA to provide notice of a significant reduction in the rate of future accrual. Pursuant to Reorganization Plan No. 4 of 1978 (1979-1 C.B. 480), questions regarding section 204(h)(1) should be directed to the Internal Revenue Service.