

U.S. Department of Labor

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



Reply to the Attention of:
John Hunter 202-523-8671

OPINION NO. 83-18A
Sec. 408(b)(4)

APR 15 1983

Mr. Ronald W. Powell
Counsel
Investors Diversified Services, Inc.
IDS Tower
Minneapolis, Minnesota 55402

Re: Employees' Incentive and Thrift Plan of Investors Diversified Services, Inc.
and its Subsidiary and Associated Companies (Plan)
Identification Number: F-2381A

Dear Mr. Powell:

This letter responds to your May 4, 1982, request for an advisory opinion under the Employee Retirement Income Security Act of 1974 (ERISA) on behalf of the Plan, Investors Syndicate of America, Inc. (ISA), Investors Diversified Services, Inc. (IDS), and the IDS Incentive and Thrift Committee (Committee). Specifically, you request an opinion that ISA is a "bank or similar financial institution" within the meaning of ERISA section 408(b)(4) and that face-amount certificates issued by ISA to the Plan are "deposits which bear a reasonable interest rate" within the meaning of that section.

According to the representations and other information contained in the submission, ISA and IDS are Delaware corporations which maintain their principal place of business in Minnesota. ISA is a wholly-owned subsidiary of IDS. The Plan is sponsored by IDS and certain of its subsidiary and associated companies, including ISA. The Committee is the plan administrator of the Plan.

ISA is predominantly in the business of issuing face-amount certificates. You describe a face-amount certificate issued by ISA (Certificate, or ISA Certificate) as an instrument under which ISA promises to pay to a depositor/purchaser a fixed amount at a definite maturity date in return for a deposit. The face amount, which includes an increment for interest, is assured by ISA, and additional interest may be applied to the Certificate as determined annually by the ISA Board of Directors for the following calendar year. ISA Certificates may be surrendered by the holder at any time without penalty. ISA maintains an account in the name of each certificate-holder. Further, ISA Certificates are securities registered with the Securities and Exchange Commission (SEC) under the Securities Act of 1933. The submission includes a prospectus describing Certificates issued to the Plan.

Face-amount certificates offered by ISA are sold throughout the United States to individual investors by the IDS sales force of approximately 3,500 salespersons. ISA issues more than 95 percent of all face-amount certificates issued in the United States. There are approximately 167,000 ISA certificate-holders in the United States. As of December 31, 1981, ISA had assets valued at over \$1 billion. The Plan holds less than one percent of the face amount of all outstanding ISA Certificates.

ISA is registered with the SEC as a face-amount certificate company under the Investment Company Act of

1940. Section 28 of the Act imposes requirements specifically on face-amount certificate companies concerning, among other things, minimum certificate reserves and deposits of cash or qualified investments, and certificate surrender values. ISA also is subject to supervision and examination by the Minnesota Commissioner of Banks. Chapter 54 of Minnesota Statutes specifically provides for regulation by the Commissioner of face-amount certificate companies. This includes authority to make periodic and annual examinations of the books and accounts of such companies and to review various reports prepared by the companies pursuant to federal securities regulations. The submission includes a copy of these Minnesota statutory provisions, the banking examiner's report of the ISA examination for the year ending December 31, 1980, and ISA's Form 10-K filed with the SEC for the year ending December 31, 1981. The banking examiner's report indicates that the primary purpose of the examination was to determine if adequate certificate reserves were being maintained and if sufficient deposits of qualified assets were being held within Minnesota, or other states where required, for the protection of the certificate-holders.

ISA Certificates are not insured or guaranteed by any federal or state agency. However, you point out that ISA is required under the Investment Company Act of 1940 to maintain on deposit at all times cash or qualified investments aggregating not less than its total liability on all of its outstanding Certificates plus its capital stock requirement of \$250,000.

You state that ISA has never requested a ruling from the Internal Revenue Service (the Service) that ISA is a "bank" as defined in section 401(d)(1) of the Internal Revenue Code of 1954 (Code), relating to qualification of trusts and plans benefiting owner-employees. However, ISA has always believed such a ruling could be obtained if requested. You indicate that this view is based on a 1975 ruling of the Service that IDS was a "bank" as defined in that Code section. This ruling was based on face-amount certificates which IDS issued before 1940 and which were still outstanding at the time of the ruling. IDS has not issued new certificates since 1940.

You point out that under section 1232 of the Code, the holder of a face-amount certificate issued after December 31, 1975, is taxed on interest earned on the certificate in a manner which is consistent with the rules of taxation applied to interest earnings on certificates of deposit, time deposits and other deposit arrangements with banks, domestic building and loan associations, and similar financial institutions. In addition, you direct our attention to a discussion of similarities between traditional banks and ISA by the U.S. Court of Claims in Investors Diversified Services, Inc. v. United States, 575 F. 2d 843, 852 (1978). In that case, the Court found that it could not separate banks from ISA for purposes of Code section 265(2), relating to non-deductibility of interest on indebtedness which is incurred to purchase or carry tax-exempt obligations.

ISA Certificates currently being offered to the Plan provide a contractually assured rate of interest equal to 3 1/2% plus additional interest of 9% for a total current interest rate of 12 1/2%. No sales charges, surrender charges, advisory fees, administrative fees or other charges of any kind are made against the Plan investments in ISA Certificates. Interest, which is compounded annually, is credited to the Certificate from the date of investment to the date of surrender. For calendar years 1978 through 1981, interest was credited on ISA Certificates purchased by the Plan at rates of 8%, 8 1/2%, 9 1/2%, and 11%, respectively.

Section 408(b)(4) of ERISA provides a conditional exemption from the prohibitions of ERISA section 406 for the investment of all or a part of a plan's assets in deposits which bear a reasonable interest rate in a bank or similar financial institution supervised by the United States or a State, even though the bank or similar financial institution is a fiduciary or other party in interest of the plan.

Based upon the facts and representations contained in your submission, including that ISA is subject to regulation by the SEC under the Investment Company Act of 1940 and is subject to supervision and examination by the Minnesota Commissioner of Banks, it is the conclusion of the Department of Labor that

ISA is a "bank or similar financial institution" within the meaning of section 408(b)(4) of ERISA.

Regulation section 29 CFR 2550.408b-4(c)(3) provides that the term "deposits" includes any account, temporary or otherwise, upon which a reasonable rate of interest is paid, including a certificate of deposit issued by a bank or similar financial institution. We believe that the ISA Certificates described by the submission are a type of deposit instrument for purposes of ERISA section 408(b)(4). A determination as to whether a particular deposit instrument provides a reasonable interest rate requires a factual analysis. Section 5.01 of ERISA Procedure 76-1 states that the Department ordinarily will not issue advisory opinions on questions of an inherently factual nature. However, assuming that ISA Certificates issued to the Plan provide a reasonable rate of interest, we conclude that they constitute "deposits which bear a reasonable interest rate" within the meaning of ERISA section 408(b)(4).

The questions you presented relate also to section 4975(d)(4) of the Code, which section corresponds to section 408(b)(4) of ERISA. Reorganization Plan No. 4 of 1978 (43 FR 47713, October 17, 1978) transferred, with certain exceptions not here relevant, the authority of the Secretary of the Treasury to issue rulings under section 4975 of the Code to the Secretary of Labor. Therefore, the views provided above apply also to that section of the Code.

This letter is an advisory opinion under ERISA Procedure 76-1. Section 10 of the Procedure describes the effect of advisory opinions.

Sincerely,

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