

U.S. Department of Labor

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



Reply to the Attention of:
Pension and Welfare Benefit Programs

OPINION NO. 83-42A
Sec. 3(1), 3(2)

AUG 17 1983

Mr. David T. Mitzner
Holme Roberts & Owen
1700 Broadway
Denver, Colorado 80290

Dear Mr. Mitzner:

This is in reply to your letter of January 8, 1982, enclosing an advisory opinion request dated December 18, 1981, concerning applicability of the Employee Retirement Income Security Act of 1974 (ERISA) to the Production Participation Plan (the Plan) of Cibola Energy Corporation (the Corporation). Specifically, you request an advisory opinion that the Plan is not covered under title I of ERISA.

The following facts and representations were contained in your request and the accompanying plan document or obtained in a phone conversation with Ms. Carolyn Daniels, a member of your staff. Under the Plan the Corporation allocates the royalties from certain oil and gas leases to a subsidiary formed for that purpose. To represent the right to receive income thus produced, the Corporation's directors assign royalty points to individuals. Payments from the Plan are made yearly to individuals prior to termination of employment and may be continued after termination of employment for some individuals. Corporation directors may appoint a separate Committee (the Committee) to administer the Plan or may itself act as the Committee.

The stated purpose of the Plan is to provide profitability incentives to employees and to enable the Corporation to attract, motivate, and retain valuable employees. The Corporation put the Plan into effect January 1, 1981. The Corporation has no retirement plan.

Each February following the end of a Plan year, the directors of the Corporation assign royalty points to individuals connected with the Corporation. Participants to whom royalty points are assigned may include employees, consultants, or persons on leave of absence. At the present time, however, no decision has been made to include any particular independent contractor in the Plan. Total royalty points assigned each year cannot be more than the total number of Corporation employees on the last day of the Plan year.

Distributions from the Plan are made yearly in lump sums after the end of each Plan year. Payments to individuals are based on the ratio of royalty points held by each participant to the total royalty points held by all participants. Cancelled royalty points are not taken into account for this purpose. Amounts distributed by the Corporation based on royalty points are made from general assets but are derived from yearly income paid over by the subsidiary to the Corporation. It is the intent of the Corporation in setting up the Plan not to create a separate fund or any ownership interests by the Plan in any properties used to

measure Plan income or in any production therefrom. Sale or transfer of production or leases being used to measure Plan income is at the discretion of the Corporation or its subsidiary with net profit paid to Plan participants. At the Corporation's sole option, it may repurchase a participant's interest in the Plan at its fair market value when such interest produces \$1000 or less income for the year.

The Plan's vesting schedule determines whether a participant may receive payments from the Plan after terminating employment. A participant's royalty points are cancelled on termination of employment prior to completion of 5 years of service, and no further payments are made to the former participant. On termination with more than 5 years of service, a participant retains a vested percentage of royalty points according to the Plan's schedule of vesting, and distributions to the participant from the Plan continue for various periods of time after termination based also on a Plan schedule which takes into account the participant's vested percentage. The Plan's schedules for vesting and for duration of distributions after termination are as follows:

Years of service:	Vested Percentage:	Number of years after termination during which payments are made:
5	20	5
10	40	10
15	60	15
20	80	20
30	100	Indefinitely

Each Plan participant files a designation of beneficiary with the Corporation, and the Plan provides that, in case of a participant's death before benefits due the participant are fully paid out, the Plan continues to pay benefits to the participant's beneficiary or personal representative. Plan participants killed or permanently disabled while on Corporation business before being fully vested are credited with 30 years of employment credit and thereby become 100 percent vested. They, their beneficiaries, or their personal representatives are thus entitled to receive distributions from the Plan indefinitely.

Under the Plan's provisions, the Corporation may terminate the Plan at any time with notice to all participants and beneficiaries. On termination of the Plan, the Corporation's directors or its subsidiary have several alternatives as follows: (1) the present worth of the participant's interest in the Plan can be distributed in a lump sum or five annual installments with interest; (2) distributions can be continued in the same manner as the Plan used prior to termination; or (3) a transfer of actual royalty interests in proportion to royalty points can be made.

Forfeiture of benefits under the Plan is provided for participants who fail to make known their addresses to the Committee within 3 years after notice by the Committee. The Plan's anti-assignment clause provides that a participant may assign this interest in the Plan to the Corporation as security for a loan but may make no other assignment of interest.

You reference ERISA Opinion 77-26A for its factual situation which you describe as similar to that under which the Plan operates in that benefits are paid currently.

The term "employee benefit plan" is defined in section 3(3) of ERISA as "... an employee welfare benefit plan or an employee pension benefit plan or a plan which is both an employee welfare benefit plan and an employee pension benefit plan." The term "employee welfare benefit plan" is defined in section 3(1) of ERISA as "... any plan, fund, or program which was heretofore or is hereafter established or maintained by an employer or by an employee organization, or by both, to the extent that such plan, fund, or program was established or is maintained for the purpose of providing for its participants or their beneficiaries, through the purchase of insurance or otherwise, (A) medical, surgical, or hospital care or benefits, or benefits in the event of sickness, accident, disability, death or unemployment, or vacation benefits, apprenticeship or other training programs, or day care centers, scholarship funds, or prepaid legal services, or (B) any benefit described in section 302(c) of the Labor Management Relations Act, 1947 (other than pensions on retirement or death, and insurance to provide such pensions)." It appears that among the purposes for which the Plan provides benefits is the occurrence of death or disability of a participant while on Corporation business. Death and disability benefits are among those enumerated in section 3(1) of ERISA. Accordingly, it is our view that the Plan is a welfare plan within the meaning of section 3(1) of ERISA. In reaching this conclusion, we have considered as especially significant the facts that (1) a participant who is killed or permanently disabled while on Corporation business is credited with 30 years of employment credit, the effect of which is described above, and (2) royalty points represent an entitlement to income not limited to that derivable from identified wells or projects, but, rather, representing a participation in an open-ended pool.

The term "employee pension benefit plan" is defined in section 3(2)(A) of ERISA as "... any plan, fund, or program which was heretofore or is hereafter established or maintained by an employer or by an employee organization, or by both, to the extent that by its express terms or as a result of surrounding circumstances such plan, fund, or program -- (i) provides retirement income to employees, or (ii) results in a deferral of income by employees for periods extending to the termination of covered employment or beyond"

Regulations issued by the Department of Labor clarify the definition of employee pension benefit plan. Concerning bonuses for work performed, 29 C.F.R. §2510.3-2(c) of the regulations provides as follows:

For the purposes of Title I of the Act and [29 C.F.R. c. XXV], the terms "employee pension benefit plan" and "pension plan" shall not include payments made by an employer to some or all of its employees as bonuses for work performed, unless such payments are systematically deferred to the termination of covered employment or beyond, or so as to provide retirement income to employees.

In view of (1) the open-ended nature of the pool that provides royalty income to Plan participants, and (2) characteristics of the Plan's vesting schedule, summarized above, which appears to allocate the economic benefits of the Plan disproportionately to retirees and participants approaching retirement age with many years of service, we are unable to conclude either that the Plan is not a pension plan covered by title I of ERISA or that it is a bonus plan described in regulation section 2510.3-2(c). We do not view this opinion as inconsistent with ERISA Opinion 77-26A to which your correspondence refers.

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

Sincerely,

Jeffrey N. Clayton
Administrator
Pension and Welfare Benefit Programs