U.S. Department of Labor **Employee Benefits Security Administration**
Washington, D.C. 20210

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ERISA SEC.
29 CFR 2510.3-101(f)

Ms. Andree M. St. Martin
Mr. Stephen M. Saxon
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Washington, D.C. 20006-5893

Dear Ms. St. Martin and Mr. Saxon:

This is in response to your request, on behalf of several insurance companies (insurers), for an advisory opinion under the Employee Retirement Income Security Act of 1974, as amended (ERISA). In particular, you ask how the significant participation test in the Department's plan assets regulation (29 CFR § 2510.3-101(f)) should be applied to an investment in an entity by a wholly owned subsidiary of an insurer's general account which holds plan assets for purposes of determining whether that entity holds plan assets.

You explain that some of the insurance and annuity contracts issued to customers by an insurer provide benefits backed by reserves held in the insurer's general account. The insurer invests general account assets in all manner of investments, and in some instances may invest those assets through wholly owned direct and indirect subsidiaries[1] that are established for business reasons unrelated to ERISA, such as limiting the recourse of a subsidiary's creditors to the investment assets of the subsidiary alone rather than to all the insurer's general account assets. You represent that under these circumstances, the assets held by the insurer's wholly owned subsidiary support the liabilities of the insurer's general account. You further represent that neither the insurer's equity interest in the subsidiary nor the assets of the subsidiary are allocated to a "separate account."

You also explain that the insurer's interest in the subsidiary, and ultimately the subsidiary's assets, would be available to satisfy the insurer's creditors in the event of insolvency because the insurer's interest in the subsidiary would be included in the insurer's estate.[2] You make representations to the effect that, for purposes of applying any limitations under state insurance law relating to investments made by the insurer,

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[1] You explain that for business reasons unrelated to ERISA (*e.g.*, to comply with constraints on investment in certain jurisdictions, such as Korea, which require all limited liability companies to have two or more owners), the insurer may invest through an indirectly wholly owned subsidiary. In that case, you represent, the subsidiary would be owned primarily by the insurer's general account, with the remaining equity interests held by another wholly owned subsidiary of the insurer.

[2] *See* N.J. Stat. Ann. § 17B:32-31 *et. seq.*; Conn. Gen. Stat. Ann. § 38a-903 *et. seq.*; N.Y. Ins. Law § 7401 *et. seq.*

the subsidiary's investments are treated as investments made by the insurer.[3] You also represent that for federal and state tax purposes, a subsidiary wholly owned by the insurer's general account is completely disregarded and its transactions and assets will be consolidated with the insurer's for tax reporting purposes, and that for purposes of GAAP accounting, the assets of the subsidiary will be consolidated with, and treated as if they are, assets of the insurer.

The plan assets regulation defines when a plan's investment in another entity causes that entity's underlying assets to be "plan assets." The plan assets regulation imposes a "look-through rule" based on the premise that, with certain exceptions, when a plan indirectly retains investment management services by investing in a pooled investment vehicle, the assets of the vehicle should be viewed as plan assets and managed according to the fiduciary responsibility provisions of ERISA.

The plan assets regulation provides at 29 CFR § 2510.3-101(a)(2) that, in the case of a plan's investment in an equity interest of an entity, the plan's assets include both the equity interest and an undivided interest in each of the underlying assets of the entity unless equity participation in the entity by benefit plan investors is not "significant," the entity is an operating company, or the equity interest held by the plan is a publicly-offered security or a security issued by an investment company registered under the Investment Company Act of 1940. Under the "significant participation" test in 29 CFR § 2510.3-101(f)(1), equity participation in an entity by benefit plan investors is "significant" on any date if, immediately after the most recent acquisition of any equity interest in the entity, 25 percent or more of the value of any class of equity interests in the entity is held by benefit plan investors (as defined in 29 CFR § 2510.3-101(f)(2)). For purposes of this determination, the value of any equity interests held by a person (other than a benefit plan investor) who has discretionary authority or control with respect to the assets of the entity or any person who provides investment advice for a fee (direct or indirect) with respect to such assets, or any affiliate of such a person, must be disregarded. 29 CFR § 2510.3-101(f)(1). 29 CFR § 2510.3-101(f)(2)(iii) provides that a "benefit plan investor" includes any entity whose underlying assets include plan assets by reason of a plan's investment in the entity.

The plan assets regulation does not expressly address the application of the significant participation test to investments by an insurance company general account. Under section 401(b) of ERISA, if an insurance company issues a "guaranteed benefit policy" to a plan, the assets of the plan are deemed to include the policy, but do not, solely by reason of the issuance of the policy, include any assets of the insurer. However, in its decision in *John Hancock Mutual Life Insurance Co. v. Harris Trust & Savings Bank*, 510 U.S. 86 (1993) (*Harris Trust*), the Supreme Court interpreted the meaning of "guaranteed

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[3] *See* N.Y. Ins. Law § 1704(d); *see also* N.J. Stat. Ann. § 17B:20-4(d) and Conn. Gen. Stat. Ann. § 38a-102d(a)(2).

benefit policy," as defined in ERISA section 401(b)(2)(B), and held that a contract qualifies as a guaranteed benefit policy only to the extent that it allocates investment risk to the insurer. Under the reasoning of this decision, an insurer's general account would be treated as holding plan assets to the extent it contains funds which are attributable to any non-guaranteed components of contracts with employee benefit plans. Prior to *Harris Trust*, the Department had taken the position in ERISA Interpretive Bulletin 75-2, 29 CFR § 2509.75-2, that if an insurance company issued a contract or policy of insurance to a plan and placed the consideration for such contract or policy in its general account, the assets of such account would not be considered plan assets.[4]

Following the *Harris Trust* decision, concerns were raised regarding its impact on the insurance companies themselves, and also on the entities in which insurance companies invest general account assets. Specifically, it was noted that, prior to *Harris Trust*, entities in which insurance companies invested general account assets might have operated under the assumption that general account assets were not plan assets, and that general accounts therefore would not be benefit plan investors under 29 CFR § 2510.3-101(f)(2)(iii). After the *Harris Trust* decision, however, entities could no longer follow this assumption. Treating insurance company general accounts as benefit plan investors could result in an increased number of entities that hold plan assets under the significant participation test, especially given that insurance company general account investments have comprised a significant source of capital investment.[5]

Responding to these concerns, the Department interpreted the plan assets regulation with respect to general account investments and expressed its view that, for purposes of determining whether equity participation in an entity by benefit plan investors is significant within the meaning of the significant participation test contained in 29 CFR § 2510.3-101(f), only the *proportion* of an insurance company general account's equity investment in the entity that represents plan assets should be taken into account. The proportion of that investment that represents plan assets would equal the proportion of the insurance company general account as a whole that constitutes plan assets.[6] For example, if an insurance company general account, 10 percent of whose assets constitute plan assets, held 50 percent of the value of equity interests in an entity, then in applying the significant participation test to that entity, 5 percent (*i.e.*, 10 percent of 50 percent) of the value of equity would be considered held by a benefit plan investor by reason of the general account's investment.[7]

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[4] *See* 61 Fed. Reg. 33847 (July 1, 1996) (removing 29 CFR § 2509.75-2(b)).

[5] *See generally* 59 Fed. Reg. 43134 (Aug. 22, 1994) (preamble to Proposed Prohibited Transaction Class Exemption 95-60 (Application No. D-9662)); 60 Fed. Reg. 35925 (July 12, 1995) (preamble to Prohibited Transaction Class Exemption 95-60); 62 Fed. Reg. 66908 (Dec. 22, 1997) (preamble to proposed regulation section 29 CFR § 2550.401c-1).

[6] 59 Fed. Reg. 43136 n.4; *see also* 60 Fed. Reg. 35930.

[7] *See* 60 Fed. Reg. 35930.

Your question essentially focuses on whether this interpretation would be applicable to the investment in an entity by the insurance company general account's wholly owned subsidiary.

You represent in this context, among other things, that the assets of such a subsidiary that is wholly owned by an insurer through its general account support the liabilities of the insurer's general account and are available to meet the claims of the insurer's general creditors in the event of the insurer's insolvency, and that neither the insurer's equity interest in the subsidiary nor the assets of the subsidiary are allocated to a separate account. You further represent that the assets of the subsidiary are treated as the assets of the insurer for purposes of state insurance law investment restrictions and GAAP accounting rules, and that the subsidiary is completely disregarded for federal and state taxation purposes. It is our view that, for purposes of applying the significant participation test to an entity in which such a subsidiary invests, the subsidiary is disregarded and the equity interest held by the subsidiary is treated as held by the insurance company's general account provided such subsidiary is wholly owned at all times during the period of such entity's existence.

This letter constitutes an advisory opinion under ERISA Procedure 76-1, 41 Fed. Reg. 36281 (1976). Accordingly, this letter is issued subject to the provisions of that procedure, including section 10 thereof, relating to the effect of advisory opinions.

Sincerely,

Louis J. Campagna
Chief, Division of Fiduciary Interpretations
Office of Regulations and Interpretations