

U.S. Department of Labor

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



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98-07A
PTE 92-06

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Dear Messrs. Schachter and Sun:

This is in response to your request for an advisory opinion concerning the applicability of Prohibited Transaction Exemption (PTE) 92-6, (57 FR 5189, February 12, 1992), to various transactions described in your request.

You have requested guidance with respect to the following three questions relating to PTE 92-6:

- (1). Whether two or more relatives of the insured will be deemed, for purposes of PTE 92-6, to be a "relative", so that a plan sale to such multiple relatives who are the sole life insurance beneficiaries will be deemed a sale to a "relative" who is the life insurance beneficiary under the contract.
- (2). Whether a life insurance contract under which the plan participant and the spouse of the participant are both insured will be deemed, for purposes of PTE 92-6, the plan's sale of an "individual life insurance....contract", where it is permissible under applicable law and under the terms of the plan for the plan to purchase and hold insurance on the life of a plan participant and his or her spouse.
- (3). Whether the sale by a plan of part, but not all, of its interest in a life insurance contract where, following such sale, the interest retained by the plan and the interest held by the purchaser will each have all of the characteristics of a separate life insurance contract, and will qualify as a life insurance contract under applicable state law, will be deemed, for purposes of PTE 92-6, to be the plan's sale of an "individual life insurance contract".

PTE 92-6 provides, in relevant part, that the restrictions of sections 406(a) and 406(b)(1) and (2) of the Employee Retirement Income Security Act of 1974 (ERISA) and the taxes imposed by section 4975(a) and (b) of the Internal Revenue Code of 1986 (the Code) by reason of section 4975(c)(1)(A) through (E) of the Code, shall not apply to the sale of an individual life insurance or annuity contract by an employee benefit plan to (1) a participant under such plan; (2) a relative of a participant under such plan; (3) an employer, any of whose employees are covered by the plan; or (4) another employee benefit plan, if -

- (1) Such participant is the insured under the contract;
- (2) Such participant is a "relative" as defined in section 3(15) of ERISA (or is a "member of the family" as defined in section 4975(e)(6) of the Code), or is a brother or sister of the insured (or a spouse of such brother or sister), and is the beneficiary under the contract;
- (3) The contract would, but for the sale, be surrendered by the plan;

(4) With respect to sales of the policy to the employer, a relative of the insured or another plan, the participant insured under the policy is first informed of the proposed sale and is given the opportunity to purchase such contract from the plan, and delivers a written document to the plan stating that he or she elects not to purchase the policy and consents to the sale by the plan of such policy to such employer, relative or other plan;

(5) The amount received by the plan as consideration for the sale is at least equal to the amount necessary to put the plan in the same cash position as it would have been in had it retained the contract, surrendered it, and made any distribution owing to the participant of his or her vested interest under the plan; and

(6) With regard to any plan which is an employee welfare benefit plan, such plan must not, with respect to such sale, discriminate in form or operation in favor of plan participants who are officers, shareholders, or highly compensated employees.

1. It is the view of the Department of Labor (the Department) that PTE 92-6 is applicable to a sale to multiple relatives, as defined in section 3(15) of ERISA, of the insured who are the sole beneficiaries under the contract, provided that all other conditions of the exemption are met.

The Department has previously noted that a plan may want to sell individual life insurance or annuity contracts to a relative of the insured for a number of reasons, including the insured's desire to preserve a valuable policy where the insured has a medical impairment and may be currently uninsurable or otherwise is unable to replace that insurance policy at standard rates in the open market. PTE 77-8, Preamble, Proposed Exemption, 42 FR 4036 et seq. (January 21, 1977); PTE 92-6, Preamble, Proposed Exemption, 56 FR 31679 et seq. (July 11, 1991). It is the view of the Department that these considerations are equally applicable to the sale of individual life insurance policies to more than one relative. Therefore, the use of the term "relative" in PTE 92-6 may be interpreted to include more than one relative.

2. It is the view of the Department that a life insurance contract covering the life of a plan participant and the life of his or her spouse would constitute an "individual life insurance ...contract", the sale of which would be exempt under PTE 92-6, assuming all conditions of the exemption are satisfied.¹

Your inquiry also seeks guidance on the scope of the term "individual life insurance contract". The Preamble to Proposed Exemption PTE 77-8 suggests that the term "individual life insurance contract" refers not to the number of individuals insured under the policy, but rather is intended to distinguish the type contract covered by the exemption from a group contract.² Furthermore, under ERISA section 514(b)(2), the scope of an individual life insurance contract offered by an employee benefit plan is governed by state law. It appears that to the extent that state law would permit an individual life insurance contract to cover the life of the participant and the participant's spouse, the Department would deem such a contract to be "an individual life insurance contract" for purposes of PTE 92-6.

3. With respect to the sale of a partial interest by a plan of a life insurance contract, you represent that there may be a variety of reasons for a plan to dispose of an interest in a life insurance contract (but not the entire contract), as well as for a participant to purchase such an interest from a plan. For example, a plan may become unable to support the

¹ We are assuming, for purposes of this opinion, that applicable law and pertinent plan provisions permit the acquisition and holding by a plan of a life insurance policy covering the lives of a participant and his or her spouse.

² Example 2 in the Preamble to Proposed Exemption PTE 77-8 (42 FR at 4037, January 21, 1977) states that a plan may decide "to convert its funding method from individual policies to a group contract".

entire contract because contributions to the plan have decreased or ceased, the contract is becoming too significant a portion of the plan's assets to be prudently maintained in its entirety under the plan, or the contract's insured is no longer insurable on the same basis as when the contract was purchased. However, the plan may be able to support a smaller contract, and it may be prudent to do so. At the same time, the participant may wish to purchase the interest that the plan is giving up. A participant's reasons for the purchase of a partial interest may include the desire to lower costs by purchasing an existing contract rather than a new one, or to preserve options available under the existing contract that may otherwise no longer be available. If the contract were not divisible and the plan could no longer maintain it in its entirety, the plan would have to dispose of the entire contract by either (1) surrendering the entire contract, or (2) selling the entire contract in a transaction covered under PTE 92-6. You represent that, because these are the only two options, a sale of the entire contract would meet condition (3) of PTE 92-6, above, that the contract would, but for the sale, be surrendered by the plan.

You believe that if the contract that the plan could no longer maintain in its entirety is divisible into two separate interests, such that one interest could continue to be maintained by the plan and the other interest could be surrendered, then a similar analysis should apply to the latter interest. With respect to that interest, the plan would likewise have to choose one of two options: (1) surrender the interest, or (2) if permissible under PTE 92-6, sell the interest in a transaction covered by that class exemption. Thus, with respect to such interest in the contract, you state that, but for the sale, the interest would be surrendered by the plan. You have stipulated that you are seeking an opinion from the Department only for the circumstance where, at the time of the sale, the interest maintained in the plan and the interest sold have all of the characteristics of separate life insurance contracts, are independently viable as life insurance contracts, could be purchased in the marketplace as life insurance contracts, and in fact qualify as life insurance contracts under applicable state law.

As stated above, under ERISA section 514(b)(2), the scope of an individual life insurance or annuity contract offered by an employee benefit plan is governed by state law. Based upon the facts and representations contained in your submissions, it is the view of the Department that the sale by a plan of an interest in an individual life insurance contract, where both the interest retained by the plan and the interest sold qualify as life insurance contracts under applicable state law, would constitute a sale of an "individual life insurance.... contract" within the meaning of PTE 92-6. Accordingly, such sale would be exempt under PTE 92-6, assuming all conditions of the exemption are satisfied.

This letter constitutes an advisory opinion under ERISA Procedure 76-1 and is issued subject to the provisions of that procedure, including section 10, relating to the effects of an advisory opinion. We note that pursuant to section 5 of ERISA Procedure 76-1 this advisory opinion relates solely to the proposed transactions described in your letter.

Sincerely,

Ivan L. Strasfeld
Director
Office of Exemption Determinations