COMMODITY FUTURES TRADING COMMISSION
2033 K STREET, N.W., WASHINGTON, D.C. 20581

DIVISION OF
TRADING AND MARKETS

T&M No. 87-11

December 4, 1987

Re: CPO Relief for the Board of a Church Plan.

Dear :

This is in response to your letter dated July 7, 1987, as supplemented by your letter dated November 2, 1987 and telephone conversations among you and your associate and Division staff, wherein you requested on behalf of the Board of "X" Church relief from commodity pool operator ("CPO") regulation with respect to its operation of certain employee retirement plans (the "Plans").

Based upon the representations made in your July 7 letter, as supplemented, we understand the facts to be as follows:

> The Board
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> The Board was incorporated in [the early 1900s] by a special Act of the State of New York for the purpose, among others, of providing retirement benefits to ministers and missionaries of the "X" denomination (the "denomination"). [Subsequently,] the Board's Act of Incorporation was amended to enable the Board to extend such benefits to the denomination's lay employees. The Board is one of [several] Related Boards of [the Church]. . . .
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> The closeness of the relationship between the Board and the Church is illustrated by the fact that, under the Board's Act of Incorporation and By-Laws, all but three of the Board's 20 Managers (i.e., directors) are elected by the Church's General Board or by the other Related Boards. The three remaining Managers of the Board are elected, by the members of the Board, from the general public on the basis of particular skills helpful

to the Board in performing its functions. The Board presents a written annual report to the Church, and the Church has the power to instruct the Board in respect to its general policies. . . . Each proposed amendment to the Board's By-Laws is required to be provided to the Church . . . at least 15 days prior to the date of the meeting at which a vote is taken. . . .

Accordingly, although it is separately incorporated, the Board is an integral part of the Church. As such, and on the basis of the Board's own purposes and operations, the Board is exempt from Federal income taxation as a religious organization described in Section 501(c)(3) of the Internal Revenue Code of 1986, as amended. . . .

The Plans

[T]his letter relates to three defined contribution retirement plans which are maintained by the Board. . . .

Each of the Plans is both a "pension plan" and a "church plan" within the meaning of Sections 3(2) and 3(33), respectively, of the Employee Retirement Income Security Act of 1974, as amended ("ERISA"). As church plans, the Plans are exempt from the requirements of Titles I and IV of ERISA. ERISA §§4(6)(2), 4021(b)(3).

The first plan is the basic retirement program of the denomination and provides variable annuities based upon individual accounts of the participating members. Contributions to this plan are made by the employing churches and other affiliated organizations of the Church on behalf of their participating employees. There are approximately 4,000 participating employer organizations . . . and approximately 11,460 participants. . . .

Since this plan is noncontributory, the Board established two supplemental retirement programs . . . to enable participants to elect to set aside from their salaries, on a tax-deferred basis, additional amounts for their retirement. There are approximately 1,282 participants in one [and] there are 195 participant accounts in the other.

> . . . [As of December 31, 1986] [t]he total assets of the three Plans amounted to $627,222,908. A portion ($619,676,990) of these assets, along with a portion ($135,459,740) of the assets of the Board that are held for its other purposes, have been combined for investment purposes in a Fund. . . . The total assets of the Fund amounted to $755,136,730 as of December 31, 1986. . . .
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> The Finance Committee of the Board appoints the investment managers, monitors their performance, determines the portion of the Fund that is to be managed by each manager, determines the investment objectives and guidelines to be followed by the managers and determines the portion of each manager's account that is to be invested (within specified limits) in fixed income, equity or other types of investment.
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> . . . .
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> After study of the potential uses of financial futures and options, one investment manager has recommended that such instruments be included in the fixed income portion of the account which it manages for the Board. At December 31, 1986, such account consisted of a portfolio of stocks, bonds and cash equivalents having a fair market value of approximately $180,000,000. Of this amount, approximately 31 percent was represented by fixed income investments. The investment manager believes that the use of such futures and options could help to limit interest rate risk in the Board's bond portfolio. It believes that the Board will not incur greater risk through the use of financial futures or options than would normally be incurred in a portfolio composed of cash-market securities exclusively. . . . 1/

As you are aware, Rule 4.5, 17 C.F.R. §4.5 (1987), provides relief from CPO regulation for the eligible persons named therein with respect to their operation of certain qualifying entities. This relief generally is

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1/ For the purpose of this letter we have not made any determination on the relative risks of the Board's contemplated commodity interest trading. Accordingly, the position we have taken below should not be construed to imply any such determination.

effective upon the filing of a notice of eligibility with the Commission, which must contain certain representations on how the qualifying entity will be operated -- e.g., that it will commit no more than five percent of its assets to initiate its commodity interest positions and that those positions will be "bona fide hedging transactions and positions" or, with respect to certain long positions, will be incidental to the qualifying entity's activities in the underlying cash market.

Specifically, Rule 4.5(a)(4) makes this relief available for the trustee or named fiduciary of a pension plan that is subject to Title I of ERISA with respect to its operation of such plan. Rule 4.5(a)(4) further provides, however, that certain pension plans are not commodity pools and, thus, that no notice of eligibility needs to be filed -- i.e., the relief provided by the rule is self-executing and is not subject to any operating criteria. Those plans are as follows: (i) a noncontributory plan covered under Title I of ERISA; (ii) a contributory defined benefit plan covered under Title IV of ERISA; and (iii) a plan defined as a governmental plan in Section 3(32) of Title I of ERISA. But because, as is noted above, as church plans the Plans are exempt from the requirements of Titles I and IV of ERISA, neither the fiduciary or named trustee of any Plan is eligible to claim relief from CPO regulation under Rule 4.5(a)(4) nor is any Plan eligible for exclusion from the pool definition under either Rule 4.5(a)(4)(i) or Rule 4.5(a)(4)(ii). Accordingly, you have requested that we exclude the Plans from the pool definition on grounds similar to those under Rule 4.5(a)(iii) upon which the Commission excluded certain governmental plans: considerations of federalism. As the Commission stated in adopting that exclusion:

> State and local governments must be allowed to make their own determination of the best method to protect the pension rights of municipal and state employees. These are questions of state and local sovereignty and the Federal government should not interfere. 50 Fed. Reg. 15868 at 15873 (April 23, 1985) (quoting 1 Legislative History of the Employee Retirement Income Security Act of 1974, 97th Cong., 2d Sess. 224 (Comm. Print 1976)).

In support of the requested relief, by your November 2 letter you represented the following:

> With respect to the ERISA church plan exemption, there appears to be only one statement in the pre-enactment legislative history regarding the reasons underlying the exemption. Such statement . . . explains why church plans were not made subject to the plan termination insurance system established by Title IV of ERISA. . . .

Following the enactment of ERISA, it became apparent to many churches that the ERISA language defining an exempt church plan was so narrowly drafted that many church plans would be unable to comply with such language [and] . . . church plans would be prevented from covering many ministers and lay workers who were engaged in carrying on the work of the church as employees of denominational agencies. . . .

[C]larifying legislation was enacted in 1980 as Section 407 of the Multiemployer Pension Plan Amendments Act of 1980 (P.L. 96-364, 96th Cong., 2d Sess.) ("MPPA"). . . .

In 1978, in introducing the House bill which was the predecessor to Section 407 of MPPA, Representative Barber Conable stated:

> In 1974 when we enacted the Employee Retirement Income Security Act of 1974, popularly called ERISA, we exempted church plans from the provisions of the act <u>to avoid excessive Government entanglement with religion in violation of the first amendment to the Constitution</u>.
>
> Mr. Speaker, I believe that when we enacted ERISA, we required far more of our churches than we intended. We certainly did not in 1974 intend to draft a definition of church plan that fails to take into consideration the way our church plans are operated <u>or that is disruptive of church affairs</u>. 124 Cong. Rec. 12,108 (1978) (emphasis added).

A similar bill was introduced in the Senate in 1978. Because Congress did not act upon the House and Senate bills prior to its adjournment in 1978, the bills were reintroduced in the House and the Senate when the new congress convened in 1979. . . . In explaining the purpose of the bill to the Senate, Senator Talmadge stated:

> . . . .
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> Mr. President, these and other problems over the church plan definition under

> present law confront the churches today. They are worried that their plans do not now meet the church plan requirements and concerned over the impending restructuring of their plans. It is time we remove the churches from this statutory cloud. If we have enacted a statute that may require the church plans to come under ERISA, file reports, be subject to the examination of books and records and possible foreclosure of church property to satisfy plan liabilities, it must be changed because we have clearly created an excessive Government entanglement with religion. 125 Cong. Rec. at 10,052 (1979) (emphasis added).

On December 4, 1979, hearings on the Senate bill were held before the Subcommittee on Private Pension Plans and Employee Fringe Benefits of the Committee on Finance of the Senate. Senator Talmadge's statement in support of the bill included the following:

> In drafting the Employee Retirement Income Security Act of 1974, which is called ERISA, Congress recognized that there were serious Constitutional objections to subjecting the churches, through their plans, to the examination of books and records and possible levy on church property to satisfy plan liabilities. As a consequence, "church plans" were excluded from the purview of ERISA. Hearings on S. 209, Etc. Before the Subcomm. on Private Pension Plans and Employee Fringe Benefits of the Senate Comm. on Finance, 96th Cong., 1st Sess. 364 (1979).

Based upon the foregoing, we believe that relief from CPO regulation is appropriate with respect to the instant case. But because the Plans are not among those specified in Rule 4.5 (either as being qualifying entities or excluded from the pool definition) and, further, because the Plans will not be operated pursuant to the criteria of Rule 4.5(c)(2), we are declining to make the relief available under Rule 4.5 available to the Board and the

Plans. 2/ Rather, the Division will not recommend that the Commission take any enforcement action against the Board of the "X" Church if it fails to register as a CPO in connection with its operation of the Plans. This position is, however, subject to compliance with the condition that the Board indicate in each Plan's documents that, as a result of its request for relief, it is neither required to register as a CPO nor is it subject to the operating criteria of Rule 4.5.

You should be aware that the "no-action" position taken by this letter does not excuse the Board from compliance with any otherwise applicable requirements contained in the Commodity Exchange Act or in the Commission's regulations thereunder. For example, it remains subject to Section 4o of the Commodity Exchange Act, 7 U.S.C. §6o (1982), and to the reporting requirements for traders set forth in Parts 15 and 18 of the Commission's regulations, 17 C.F.R. Parts 15 and 18 (1985).

The position taken by this letter is based on the representations that have been made to us and is subject to compliance with the condition set forth above. Any different, changed or omitted facts or conditions might require us to reach a different conclusion. In this connection, we request that you notify us immediately in the event any Plan's operation changes in any way from that as represented in your letter and in your telephone conversations with Division staff.

Very truly yours,

Andrea M. Corcoran
Director

BSG/md

cc: Daniel A. Driscoll, National Futures Association

2/ Compare Division of Trading and Markets Interpretative Letter No. 87-3, Comm. Fut. L. Rep. (CCH) ¶23,730 (July 14, 1987), where we found that the insurance company at issue would come within Rule 4.5; compare also Division Interpretative Letter No. 85-8, Comm. Fut. L. Rep. ¶22,728 (February 8,1985), which extended the relief proposed under Rule 4.5 to a private investment company.