Delaware Journal of Corporate Law

VOLUME 5 1980 NUMBER 3

SECTION 3(a)(2) OF THE SECURITIES ACT AFTER *DANIEL*

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IN *International Brotherhood of Teamsters v. Daniel*,[1] the Supreme Court construed section 3(a)(2) of the Securities Act of 1933[2] (1933 Act), the basic exemption from registration for employee benefit plans, in such a fashion as to cast doubt on its availability for many plans.[3] Although the 1933 Act was not before the Court, the litigants relied on the legislative history of the 1933 Act to support their arguments concerning the applicability of the Securities Exchange Act of 1934.[4] Much of the legislative history cited to the Court

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1. 439 U.S. 551 (1979).

2. 15 U.S.C. §§ 77a-77aa (1976).

3. The Court held that interests in compulsory, noncontributory pension plans providing for defined benefits are not securities. 439 U.S. at 570; *see* text accompanying notes 20-23 *infra*. Lower courts have now held that even if the defined benefit plan is voluntary and contributory, interests in the plan are not securities. Black v. Payne, 591 F.2d 83 (9th Cir. 1979); Tanuggi v. Grolier, 471 F. Supp. 1209 (S.D.N.Y. 1979); Newkirk v. General Elec. Co. [1979-80 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 97,216 (N.D. Cal. 1979). Accordingly, it would seem that defined benefit plans are not subject to the 1933 Act at all. *But see* SEC Release No. 33-6188 at 25-26 (Feb. 1, 1980), *reprinted in* 1 FED. SEC. L. REP. (CCH) ¶ 1051 [hereinafter cited as SEC Release No. 33-6188]. However, contributory defined contribution plans are still securities and noncontributory defined contribution plans may also be. *See* text accompanying notes 13-16; note 32 *infra;* SEC Release No. 33-6188, *supra* at 35-40.

4. *See* Brief for the Securities and Exchange Commission as Amicus Curiae at 59-61, International Bhd. of Teamsters v. Daniel, 439 U.S. 551 (1979) [hereinafter cited as SEC Brief]; Brief of Respondent John Daniel at 72-76, International Bhd. of Teamsters v. Daniel, 439 U.S. 551 (1979) [hereinafter cited as Plaintiff's Brief]; Brief for International Brotherhood of Teamsters at 116-34, International Bhd. of Teamsters v. Daniel, 439 U.S. 551 (1979) [hereinafter cited as Teamster's Brief].

The application of the 1933 Act to employee benefit plans and the *Daniel* case have evoked much comment. *See generally* Drisdale, *Employee Stock Ownership Plans and Securities Laws*, 32 BAYLOR L. REV. 19 (1980); Kelly, *Securities Regulation of Retirement Plans After* Daniel, 10 LOY. CHI. L.J. 631 (1979) [hereinafter cited as Kelly]; Lorne, *Accommodating the Securities Laws to Employee Benefit Plans*, 1979 DUKE L.J. 421 [hereinafter cited as Lorne]; Nimkin, *Noncontributory Benefit Plans*, 12 R. SEC. REG. 969 (1979) [hereinafter cited as Nimkin]; Stansbury

underlay the 1970 amendments[5] to section 3(a)(2). Accordingly, the Court construed section 3(a)(2) even though a construction of the Section was not necessary to reach its decision. That construction, however, departed from the prevailing Securities and Exchange Commission (SEC) and securities bar interpretation of the Section.

Prior to *Daniel,* the SEC treated employee benefit plans as involving the issuance of only one interest which could be considered a security—the employee's interest in the plan's funding vehicle.[6] Often, that security was exempted from registration by section 3(a)(2). The Court, however, indicated in dicta that two securities may exist—the employee's interest in the plan (generally called a participation) and the plan's interest in its trust or other funding vehicle.[7] Furthermore, the Court concluded that the section 3(a)(2) exemption applies *only* to the *plan's interest in its funding vehicle.* Implementation of the Court's conclusion would therefore require 1933 Act registration of any employee interests in benefit plans which, after *Daniel,* can still be considered securities.[8]

In response to *Daniel,* the SEC issued a comprehensive release revealing a new position on the registration of interests in employee benefit plans.[9] This new position is partially consistent with the Court's analysis in *Daniel;* the SEC has abandoned its previous position that only a single security exists, and has acquiesced in the Court's analysis that a benefit plan may involve two securities.[10] However, despite the Court's indication that section 3(a)(2) was applicable only to the plan's interest in its funding mechanism, the SEC concluded that section 3(a)(2) applies to *both* the employee's interest in the plan *and* the plan's interest in its funding vehicle.[11] Unfortunately, there is no support in the legislative history or in the statute for applying section 3(a)(2) to the newly created employee interest in the plan. The statute itself applies literally only to interests

& Bedol, *Interests in Employee Benefit Plans as Securities:* Daniel *and Beyond,* 8 SEC. REG. L.J. 226 (1980) [hereinafter cited as Stansbury & Bedol]; Tomlinson, *Securities Regulation of Employee Stock Ownership Plans; A Comparison of SEC Policy and Congressional Intent,* 31 STAN. L. REV. 121 (1978) [hereinafter cited as Tomlinson] and authorities cited therein at 122 n.3; Note, *Interest in Pension Plans as Securities:* Daniel v. International Brotherhood of Teamsters, 78 COLUMB. L. REV. 184 (1978).

5. Investment Company Amendments Act of 1970, Pub. L. No. 91-547, §27(b), 84 Stat. 1413 (1970); Act of Dec. 22, 1970, Pub. L. No. 91-569, §6(a), 84 Stat. 1497 (1970).

6. *See* note 33 *infra.*

7. 439 U.S. at 564-65.

8. *See* note 32 *infra* and accompanying text.

9. SEC Release No. 33-6118, *supra* note 3.

10. *Id.* at 18-19.

11. *Id.* at 90.

in trusts (although it can be fairly read to include any funding vehicle adopted by a plan).[12] If two securities exist, the Supreme Court's conclusion would seem unavoidable—section 3(a)(2) applies only to the plan's interest in its funding vehicle. Thus, registration of the employee interests in the plan would be required.

Nevertheless, the SEC's construction of section 3(a)(2) should be supported as it clearly comports with the congressional policies underlying the 1933 Act. The 1933 Act is designed to protect investors by requiring issuers of securities to disclose material information concerning the securities to potential investors. Except in those instances in which section 3(a)(2) is not available in any event—where a plan permits the purchase of employer securities with employee contributions—no meaningful disclosure will be made in registration statements covering employee interests which is not already required by the Employee Retirement Income Security Act of 1974 (ERISA).[13]

This article will analyze the Supreme Court's and the SEC's application of section 3(a)(2). It will conclude, first, that the SEC's application of section 3(a)(2) is correct, although in the opinion of this author, for the wrong reason; and second, that only one security, not two, can exist in a benefit plan, and section 3(a)(2) applies to that security. The SEC's pre-*Daniel* forty-year-old policy that only one security is present in an employee benefit plan is amply supported by the legislative history of section 3(a)(2). On the other hand, the Supreme Court's application of section 3(a)(2) arose from its creation of a hitherto unknown security, the benefit plan's interest in its own funding vehicle—a security not mentioned by Congress. If only one security is found to exist, then the application of section 3(a)(2) is straightforward and consistent with the position taken in the SEC release.

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12. *See* text accompanying note 14 *infra*.

13. 29 U.S.C. §§ 1001-1381 (1974) [hereinafter cited as ERISA]; *see* Lorne, *supra* note 4, at 439; Tomlinson, *supra* note 4, at 130-31. Section 3(a)(2) excludes plans permitting the purchase of employer securities with "amount[s] in excess of the employer's contribution." Taken literally, this phrase would exclude plans which permitted the purchase of employer stock with dividends on employer stock already in the trust. The exclusion was intended only to reach contributory plans investing participant contributions in employer stock and has been so interpreted by the SEC. *See Mutual Fund Legislation of 1967: Hearings on S. 1659 Before the Senate Comm. on Banking and Currency*, 90th Cong., 1st Sess. 1349 (1967) (memorandum of Securities and Exchange Commission) [hereinafter cited as *1967 Senate Hearings*]; *id.* (statement of American Life Convention and Life Insurance Association of America); *The ERISA Improvements Act of 1978: Joint Hearings on S. 3017 Before the Subcomm. on Labor of the Sen. Comm. on Human Resources and the Subcomm. on Private Pension Plans and Employee Fringe Benefits of the Sen. Comm. of Finance*, 95th Cong., 2d Sess. 333 (1978) (statement of Harold M. Williams, Chairman, SEC) [hereinafter cited as *1978 ERISA Improvements Act Hearings*]; *see also* note 26 *infra*.

I. SECTION 3(a)(2) AND EMPLOYEE BENEFIT PLANS

Section 3(a)(2) of the 1933 Act exempts certain classes of securities from the registration provisions of the Securities Act. In 1970 it was amended to exempt:

> [A]ny interest or participation in a single or collective trust fund maintained by a bank or in a separate account maintained by an insurance company which interest or participation is issued in connection with . . . a stock bonus, pension, or profit sharing plan which meets the requirements for qualification under section 401 of the Internal Revenue Code of 1954 . . . other than any plan . . . the contributions under which are held in a single trust fund . . . or in a separate account . . . for a single employer and under which an amount in excess of the employer's contribution is allocated to the purchase of securities (other than interests or participations in the trust . . . itself) issued by the employer . . . .[14]

To understand the scope and purpose of section 3(a)(2) a general understanding of employee benefit plans is necessary. While benefit plans vary greatly in their terms, they all involve a sponsoring entity (the employer or employee organization) establishing a plan for the exclusive benefit of its participating employees (participants).[15] All contributions under the plans are delivered to a trustee or insurance company (trustee) which holds the plan assets in a trust or separate account (trust) and invests the trust funds in accordance with the terms of the plan and trust agreement.[16] The employer or plan sponsor drafts and adopts the plan and establishes the trust. The

14. Investment Company Amendments Act of 1970, Pub. L. No. 91-547, sec. 27(b), § 3(a)(2), 84 Stat. 1413 (1970); Act of Dec. 22, 1970, Pub. L. No. 91-567, sec. 6(a), § 3(a)(2), 84 Stat. 1497 (1970).

Section 3(a)(2) was amended again in 1980 to exempt

> [a]ny interest or participation in a single trust fund, or in a collective trust fund maintained by a bank, or any security arising out of a contract issued by an insurance company, which interest, participation, or security is issued in connection with . . . a stock bonus, pension, or profit-sharing plan which meets the requirements for qualification under section 401 of the Internal Revenue Code of 1954 . . . other than any plan . . . the contributions under which are held in a single trust fund or in a separate account . . . for a single employer and under which an amount in excess of the employer's contribution is allocated to the purchase of securities (other than interests or participations in the trust or separate account itself) issued by the employer . . . .

Small Business Investment Incentive Act of 1980, Pub. L. No. 96-477 § 701 (1980). Because *Daniel* was decided before the 1980 amendment and relied heavily on the legislative history underlying the 1970 version of the statute, this article will refer to the 1970 version except where the 1980 amendments change the analysis. This is rarely the case since the 1980 amendments do not address the fundamental problems caused by the *Daniel* decision.

15. I.R.C. § 401(a)(2).

16. ERISA § 403, 29 U.S.C. § 1103 (1976).

sponsor may also select the trustee and can generally remove the trustee at will. The plan specifies who shall have discretion concerning the investment of trust funds and whether that person is permitted or required to invest trust assets in employer securities. If plan assets are to be invested in a bank maintained collective trust, it is, and has long been, almost universal practice to create a single trust which places its assets in the collective trust and itself holds an interest in the collective trust.[17]

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17. *See* Rev. Rul. 267, 1956-1 C.B. 206; Rev. Rul. 297, 1966-2 C.B. 234. *See generally* Wade, *Bank-Sponsored Collective Investment Funds: An Analysis of Applicable Federal Banking and Securities Laws*, 35 BUS. LAW. 361 (1980). *But see Communications Workers of America* (SEC no-action letter available January 27, 1980), *reprinted in* [Current Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 76,321 [hereinafter cited as *Communications Workers of America*]. The SEC has had difficulty defining the characteristics of an employee benefit plan "collective trust." It has generally been assumed that a collective trust is a trust holding the assets of more than one employee benefit plan trust—a so-called "trust of trusts." *See* Wade, *supra* at 368. However, the SEC has argued that under section 3(a)(2) a "collective trust" need not consist of the assets of more than one employee benefit plan trust, but can consist solely of the assets of the trust established under a multi-employer plan. *Communications Workers of America, supra.*

In *Communications Workers of America*, the Communications Workers of America Savings and Retirement Trust (the "Plan") described itself as a multi-employer pension plan qualified under section 401 of the Internal Revenue Code. Under the Plan, participants are employees of various unrelated employers all of whom belong to the union sponsoring the Plan. Employee participation is voluntary. The assets of the Plan are administered by a Board of Trustees consisting of union employees, employer officials and a bank, therefore for purposes of section 3(a)(2), the Plan's trust is not maintained by a bank and therefore would not literally fall within the exemption.

The Plan sought advice from the SEC that even though the Plan's trust was not maintained by a bank, the section 3(a)(2) exemption from the 1933 Act was available. The Plan based this conclusion on its argument that it is a "single trust." The SEC has on a number of occasions issued no-action letters indicating that a "single trust" need not be maintained by a bank to qualify for the section 3(a)(2) exemption. The SEC has construed the phrase "maintained by a bank" to apply only to the words "collective trust" and therefore a single trust need not be maintained by a bank. *See, e.g., New England Electric System Companies Pension Plans* (SEC no-action letter available May 7, 1979); *Gilbert Associates, Inc.* (SEC no-action letter available December 1, 1977), *reprinted in* [1977-1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 81,406; *Maremount Corporation* (SEC no-action letter available August 12, 1976). This interpretation by the SEC, while inconsistent with the language of section 3(a)(2), is a rational and practical approach and is consistent with congressional goals underlying its adoption. Indeed, in 1980 Congress amended section 3(a)(2) to reflect the SEC's position. *See* note 14 *supra*. In any event, it was important to the Plan that it be deemed a "single trust" for purposes of section 3(a)(2).

The Plan noted that under the Investment Company Act it is not a collective trust. The Investment Company Act exempts from the definition of investment company an employee benefit plan trust or a collective trust consisting solely of the assets of employee benefit plans qualified under section 401. Investment Company Act, § 3(c)(11), 15 U.S.C. § 80a-3(c)(11) (1976). *See generally Southland Trust Company* (SEC no-action letter available April 14, 1980), *reprinted in* [Current Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 76,381; *Maryland National Bank Group Trusts* (SEC no-action letter available January 9, 1980), *reprinted in* [Current Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 76,305. The Investment Company Act is explicit that only a collective trust holding other trust assets, a "trust of trusts," is included within the exclusion from the definition. Furthermore, the Plan pointed out that under the Internal Revenue Code it is not a collective trust. A collective trust can only be qualified under section 401 if it consists of the assets of trusts that are qualified under section 401.

The section 3(a)(2) exemption is available only for interests in plans with trusts qualified under section 401 of the Internal Revenue Code.[18] Major examples of these types of plans are employee stock ownership plans and thrift plans. In addition, collective trust funds holding assets only of plans qualified under section 401 are eligible for similar tax benefits[19] and are also within the section 3(a)(2) exemption.

The SEC has categorized employee benefit plans by three major variables: (a) voluntary or involuntary; (b) contributory or noncontributory; and (c) defined benefit or defined contribution.[20] Voluntary plans permit participation at the election of eligible employees while involuntary plans require employee participation. In contributory plans, employees contribute cash or other assets for investment under the plan, whereas in noncontributory plans employees may not so contribute.[21] Under a defined benefit plan, benefits are fixed or specified by formula[22] and usually provide a fixed dollar amount payable in monthly or annual installments to participants who retire at a certain age. Therefore, benefits are not based on the success of the investment policy of the plan. Contrarily, a defined contribution plan pays benefits based on the success of the investments of the plan.[23] The assets of either type of plan can be invested in the full panoply of investment media from employer stock to certificates of deposit and insurance contracts.

Notwithstanding the contrary evidence, the SEC interpreted section 3(a)(2) to apply the phrase "collective trust" to the Plan. It did so because a House Report construing section 3(c)(11) noted that the collective trust provisions were intended to refer to trusts holding the assets of more than one employee benefit plan. *See* H.R. REP. No. 1382, 91st Cong., 2d Sess. 18 (1970) (Investment Company Amendment Act of 1970). Such an interpretation of this statement in the House Report is strained at best. A much more reasonable interpretation of the House Report is simply that the House, as it has typically done, viewed plans and their trusts as single entities and therefore a collective trust was simply a trust holding the assets of a number of plans (and therefore their trusts).

The SEC's interpretation of the phrase "collective trust" in *Communications Workers of America* will cause contradictory applications of identical language appearing in the 1933 Act and the Investment Company Act. Notwithstanding this, the SEC acknowledged that the scope of the phrase "collective trust" contained in sections 3(a)(2) and 3(c)(11) was identical. The SEC would certainly have been much better served simply to have agreed with the Communications Workers Plan that it was a "single trust" as that phrase was intended in section 3(a)(2). Nothing whatever seems to have been gained by the SEC in deeming it to be a "collective trust". Indeed, such an interpretation required the SEC to further distort the application of section 3(a)(2) by adopting yet another administrative interpretation inconsistent with its language (especially as amended in 1980, *see* note 14 *supra*.) as well as casting doubt upon the hitherto clear meaning of section 3(c)(11).

18. I.R.C. § 401(a).

19. I.R.C. § 501; Rev. Rul. 267, 1956-1 C.B. 206; Rev. Rul. 297, 1966-2 C.B. 234.

20. SEC Release No. 33-6188, *supra* note 3, at 23-28.

21. *Id.* at 32-33.

22. *See* ERISA § 3(35), 29 U.S.C. § 1002(35) (1975).

23. *Id.* § 3(34), 29 U.S.C. § 1002(34).

II. THE *Daniel* INTERPRETATION OF SECTION 3(a)(2)

The *Daniel* case was ill suited for construing section 3(a)(2) because the 1934 Act antifraud provisions,[24] not the 1933 Act registration provisions,[25] were before the Court. However, plaintiff and the SEC used the 1970 amendments to section 3(a)(2) and their legislative history to support an argument that Congress intended all pension plan interests to be securities.[26] In response, the Teamsters

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24. Securities Exchange Act of 1934 § 10(b), 15 U.S.C. § 78j(6) (1976); rule 10b-5, 17 C.F.R. § 240.10b-5 (1978).

25. Securities Act of 1933 § 5, 15 U.S.C. § 77c (1976).

26. The SEC, as *amicus curiae* for the plaintiff, argued to the Seventh Circuit that "Congress has evidenced its agreement with the Commission's position that interests in pension funds are securities . . . . In codifying the 'long established administrative practice of the Commission' Congress in 1970 exempted interests in pension funds from the Securities Act's registration provisions . . . ." (citations omitted). Brief for the SEC as *Amicus Curiae* at 30, Daniel v. International Bhd. of Teamsters, 561 F.2d 1223 (7th Cir. 1977) [hereinafter cited as SEC Seventh Circuit Brief].

The Seventh Circuit adopted the SEC's argument stating:

> Congress has evidenced agreement with the SEC's position that interests in pension funds are securities by way of the Investment Companies [sic] Amendments Act of 1970. Recognizing that interests in employee pension funds are "securities," in 1970 Congress decided to exempt them from the registration requirements of Section 5 of the 1933 Act. . . . This exemption was to codify the long established administrative practice of the Commission in exempting certain pension funds from the registration requirements of the 1933 Act. H.R. REP. No. 91-1631, 91st Cong., 2d Sess. 31 (1970) [quoted in relevant part in text accompanying note 61 *infra*].

561 F.2d at 1239. *See also* Plaintiff's Brief, *supra* note 4, at 72-78; SEC Brief, *supra* note 4, at 58-63.

Notwithstanding Congress' amending section 3(a)(2) to exempt interests in trusts issued in connection with employee benefit plans, there is nothing in the legislative history to suggest that Congress believed all interests in trusts established under tax qualified pension plans to be securities. *See* letter from Senator Harrison A. Williams to Harold M. Williams, Chairman, SEC (Dec. 13, 1977), *reprinted in Oversight of ERISA, 1977: Hearings on S. 2125 Before the Subcomm. on Labor of the Sen. Comm. on Human Resources*, 95th Cong., 1st Sess. 128 (1977) [hereinafter cited as *1977 ERISA Oversight Hearings*]. The exemption was created for those pension plan interests which are securities, but it did not enlarge the categories of such interests which are securities.

The Chairman of the SEC testified in connection with section 3(a)(2) that "it is important . . . to note the nature and significance of the plans which [the 1970 amendments to section 3(a)(2)] would affect . . . . This is particularly true of corporate plans. Unlike the traditional pension plan which is [a defined benefit plan] . . . , these plans contemplate an investment in equities." *Investment Company Act Amendments of 1967, Bank and Insurance Company Collective Investment Funds and Accounts: Hearings on H.R. 14742: Before the Subcomm. on Commerce and Finance of the House Comm. on Interstate and Foreign Commerce*, 90th Cong., 2d Sess. 137 (1968) (statement of Manuel F. Cohen, Chairman, SEC) [hereinafter cited as *1968 House Hearings*]. It seems clear that defined benefit plans were not being pushed as securities by the SEC.

Indeed, Senators Javits and Williams exhibited considerable surprise when the Seventh Circuit's decision in *Daniel* included within the definition of a security defined benefit pension plans and perhaps other welfare plans which had not before been considered securities. *See 1978 ERISA Improvements Act Hearings, supra* note 13, at 322; letter from Senators Harrison A. Williams and Jacob K. Javits to Harold M. Williams, Chairman, SEC (Nov. 21, 1977), *reprinted in 1977 ERISA Oversight Hearings, supra* at 117; letter from Senator Harrison A. Williams to Harold M. Williams, Chairman, SEC (Dec. 13, 1977), *reprinted in 1977 ERISA*

argued that pension plan interests were not involved in section 3(a)(2) at all, merely benefit plan trusts and bank collective trusts holding benefit plan assets.[27] This was the position taken by the Supreme

Oversight Hearings, id. at 128. They introduced legislation to definitively remove defined benefit plans subject to ERISA from the ambit of the securities acts. S. 3017, 95th Cong., 2d Sess., 124 CONG. REC. S6581 (daily ed. May 1, 1978); S. 209, 96th Cong., 1st Sess., 125 CONG. REC. 557 (daily ed. Jan. 24, 1979), *reprinted in ERISA Improvements Act of 1979: Hearings on S. 209: Before the Sen. Comm. on Labor and Human Resources,* 96th Cong., 1st Sess. 9 (1979) [hereinafter cited as *1979 ERISA Improvements Act Hearings*].

Congress has had many occasions in the past to consider whether or not all pension plans should have been regulated under the securities acts and has apparently concluded in the negative. For example, during consideration of the Welfare and Pension Plan Disclosure Act of 1958, 29 U.S.C. § 301 (repealed 1975), considerable debate ensued as to which federal agency should administer the act. The Chairman of the SEC testified that while "the Commission would be pleased to undertake [administration of the Act] if Congress so desires," it was his personal opinion that "it would be inappropriate for the Commission to undertake this function." *Welfare and Pension Plans Legislation; Hearings on S. 1122, S. 1145, S. 1813, S. 2137, and S. 2175 Before the Subcomm. on Welfare and Pension Plans Legislation of the Senate Comm. on Labor and Public Welfare,* 85th Cong., 1st Sess. 108 (1957). The reason for this reluctance on the part of the SEC was its view that these plans did not affect the capital-securities markets and therefore were not properly within the charge given the SEC. *Id.* at 107-11. For a discussion of the interplay between the 1933 Act and ERISA, *see* Tomlinson, *supra* note 4, at 124-27, 131; letter from Senator Harrison A. Williams to Harold M. Williams, Chairman, SEC (Dec. 13, 1977), *reprinted in 1977 ERISA Oversight Hearings, supra* at 128.

It is important to note that the chairman's testimony in no way conflicts with the SEC's then 27-year-old position that plans permitting purchase of employer stock with participant contributions were securities. The distinction was the same distinction carried through in the Investment Company Amendments Act of 1970—defined benefit pension plans do not involve investments by participants, but contributions to defined contribution plans purchasing employer securities do. Since the purchase of an interest in a defined benefit plan is not the equivalent of an investment in the capital markets, participants are not in need of the disclosures required by the 1933 Act. The only effect of these plans on the capital markets is through the investment by the trust and since the participant does not have a beneficial interest in the trust assets he or she is not in need of 1933 Act protection.

One of the reasons ERISA was necessary was to insure that employers made adequate disclosures to employees with respect to benefit plans and to protect employee interests in those plans. H.R. REP. No. 533, 93d Cong., 1st Sess. 1-2, 18 (1973); *see* 439 U.S. at 569-70. The ERISA committee reports include no discussion of the role of SEC regulation of pension plans, undoubtedly because none was foreseen except in the case of defined contribution plans investing in employer securities. *See* S. REP. No. 634, 92d Cong., 2d Sess. 96-97 (1972); letter from Senator Harrison A. Williams to Harold M. Williams, Chairman, SEC (Dec. 13, 1977), *reprinted in 1977 ERISA Oversight Hearings, supra* at 128. *See generally* H.R. REP. No. 533, 93d Cong., 1st Sess. (1973); H.R. REP. No. 1280, 92d Cong., 2d Sess. (1974); Tomlinson, *supra* note 4, at 125-27. To argue that Congress believed *all* pension plan interests to be securities bordered on the incredible. *See* 439 U.S. at 566-69; *1977 ERISA Oversight Hearings, supra* at 550 (statement of George J. Pantos); letter from Senator Harrison A. Williams to Harold M. Williams, Chairman, SEC (Nov. 23, 1977), *reprinted in 1977 ERISA Oversight Hearings, id.* at 772; letter from George Meany, President, AFL-CIO, to Senator Harrison A. Williams (Nov. 18, 1977), *reprinted in 1977 ERISA Oversight Hearings, id.* at 773.

27. *Teamsters' Brief, supra* note 4, at 116, 118. The Teamsters stated:

> The 1970 amendment deals only with single and collective trust funds maintained by a bank or in separate accounts maintained by an insurance company; these it exempts from registration . . . . The amendment was drafted to deal only with the question of whether banks and insurance companies are required to register their sales of interests in trust funds . . . which they maintain in connection with employee pension plans.

Id. at 118. *See also* 561 F.2d at 1240.

Court,[28] which, in support of its analysis, adopted the Teamsters' interpretation of the legislative history underlying the 1970 amendments to section 3(a)(2).[29] Thus, the Court concluded that section 3(a)(2)'s

> central purpose . . . was to relieve banks and insurance companies of certain registration obligations. The [1970] amendment recognized only that a pension plan had "an interest or participation" in the fund in which its assets were held not that prospective beneficiaries of a plan had any interest in either the plan's bank-maintained assets or the plan itself.[30]

If this interpretation is correct, two major problems are evident. First, section 3(a)(2) is not available to exempt the issuance of participations. Underlying the Supreme Court's interpretation of section 3(a)(2) is the notion that the benefit plan trust is issuing securities separate and apart from the investment contracts being issued to participants by either the plan or the employer.[31] The trust's securities may be exempt under section 3(a)(2), but the employees' interests in the plan are not (although other exemptions may be available). Therefore, the Supreme Court's interpretation implies that employers who have not registered participations in reliance on section 3(a)(2) may be in violation of the 1933 Act.[32]

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28. 439 U.S. at 564-65. *Compare* 439 U.S. at 564-65 *with Teamsters' Brief, supra* note 4, at 116, 118.

29. 439 U.S. at 565 n.19.

30. *Id.* at 565.

31. *See* note 33 *infra.*

32. If section 3(a)(2) relates only to the trust funds and not to the investment contracts issued to employees, then a new rationale for the exemption of these participations from the registration provisions must be found or employers establishing benefit plans may be in violation of the 1933 Act. *See* Lorne, *supra* note 4, at 428-30.

While the Supreme Court has removed, by its interpretation, any statutory exemption from registration, two rationales remain for not registering the participations. After *Daniel* one could conclude that participations are not securities at all. The SEC has in fact concluded that interests in noncontributory plans and certain stock-bonus and stock-ownership plans are not securities. SEC Release No. 33-6188, *supra* note 3, at 5 n.6, 30, 72-74. In *Daniel,* interests in the pension plan were found not to be investment contracts because the employees did not invest money and had no expectation of profits from a common enterprise. 439 U.S. at 558-62. *See generally* SEC v. W. J. Howey, 328 U.S. 293 (1946). The Court found no investment of money because the pension plan was "a relatively insignificant part of an employee's total and indivisible compensation package." 439 U.S. at 560. The test appears to be whether or not the value of the employee benefits is large enough to affect an employee's decision to accept employment or stay with the employer. The Court stated that "[l]ooking at the economic realities, it seems clear that an employee is selling his labor primarily to obtain a livelihood, not making an investment." *Id.* However, the Court's economic realities seem very shortrun; many employees seek not only an immediate livelihood, but long-term post-retirement security. Employers compete for employees not only on the basis of wages but also on the basis of benefits, including retirement plans. Furthermore, plans with vesting schedules give an employee a great incentive to remain employed so that he or she can earn the greatest amount possible under the benefit plans. It seems entirely possible that

Second, by negative implication, banks acting as trustees of some contributory plans are issuing securities which must be registered under the 1933 Act. While the language of section 3(a)(2) exempts securities issued by trusts, under the Supreme Court's analysis it does so only when the contributions of participants are not being used to purchase employer securities. Thus it would seem that in some contributory plans, the plan's trust is issuing a security which is not exempt by section 3(a)(2). Someone, presumably the trustee, must therefore file a registration statement in connection with the sale of those securities if another exemption is not available. Those banks which have not registered such interests in their existing benefit plan trusts may then be in violation of the 1933 Act.

III. THE SEC'S RESPONSE TO *Daniel*

After the Supreme Court's rejection of its *Daniel* arguments, the SEC abandoned its long-held position that an employee's interest in a

faced with a defined contribution employee benefit plan with annual contributions equal to 10% of the employee's compensation and a five-year vesting schedule, the Court might find the employee to have made an investment. *See* Lorne, *supra* note 4, at 437-39. *But see* Kelly, *supra* note 4, at 649-51. Stansbury & Bedol, *supra* note 4, at 238-39.

Since benefits under defined contribution plans depend in great measure on the performance of the fund, participants would appear to have an expectation of profits from a common enterprise. *But see* Kelly, *supra* note 4, at 651-52; SEC Release No. 33-6188, *supra* note 3, at 33. Unlike the *Daniel* plan, participants in a defined contribution plan have an identifiable interest in the securities portfolio of the trust. The performance of this portfolio as managed by the trustee will determine the participant's ultimate benefits. Participants thus have an expectation of profits based on the trustee's managerial abilities. Therefore, despite the SEC's position, it is far from clear that interests in defined contribution plans are not securities.

In some stock-bonus plans it may not be necessary to analyze the interest in the plan as an investment contract to find that it is a security. In stock-bonus plans the employee's account is credited with a certain number of shares of his or her employer's stock. Once these shares are vested, the participant owns these shares and in some plans has the right to withdraw them on demand. *See, e.g.,* Tax Reduction Act of 1975, Pub. L. No. 94-12, §§ 301(d)(3), (4), (5), 89 Stat. 26 (1975). The employer's stock is without question a security, and participations are no more than beneficial interests in those securities. Hence, the participation can be a security without being an investment contract. Nimkin, *supra* note 4, at 970; *see* SEC Release No. 33-4790 (July 13, 1965), *reprinted in* 1 FED. SEC. L. REP. (CCH) ¶ 1131.

While, under *Daniel,* interests in noncontributory or involuntary plans are not securities, it may still be argued that voluntary contributory plans, even though not investing in employer securities, do issue securities. As to the latter class of plans, the prototypical example being thrift plans, the previously available exemption under section 3(a)(2) may no longer be available in light of the Court's dicta.

If the interests in a benefit plan are found to be a security, one could perhaps still avoid registration by relying on the no-sale theory as the SEC did prior to the 1970 amendment to section 3(a)(2). *See* note 33 *infra.* But there are now significant problems with returning to such a theory. *See* Lorne, *supra* note 4, at 441; Nimkin, *supra* note 4, at 970; note 33 *infra. But see* Latto, *Employee Benefit Plans—1933 Act Issues After* Daniel, in PLI ELEVENTH ANNUAL INSTITUTE ON SECURITIES REGULATION 731, 748 (1979) [hereinafter cited as Latto]. In any event the no-sale theory would be unavailable for contributory plans. In short, there do not appear to be readily available exemptions for interests in benefit plans if a two-security analysis is adopted.

plan was an interest in the benefit plan trust [33] and adopted the Court's

33. SEC Release No. 33-6188, *supra* note 3, at 18-19; *see* note 70 *infra* and accompanying text.

As early as 1941, the SEC recognized that the right to participate in a defined contribution benefit plan was a security. Opinion of Assistant General Counsel of the Securities and Exchange Commission (1941), *reprinted in* [1941-1944 Transfer Binder] FED. SEC. L. REP. (CCH) ¶75,195. The SEC took the position that the interests were investment contracts. *Id.* Sales of the participations were subject to the 1933 Act and had to be either qualified for an exemption from registration or registered under the Act.

At the same time the SEC recognized that interests in a defined contribution plan were securities, it concluded that noncontributory plans were gifts from the employer to the participant. Opinion of Assistant General Counsel of Securities and Exchange Commission (1941), *reprinted in* 1 FED. SEC. L. REP. (CCH) ¶2105.53. Since they were gifts, there was no sale of a security involved in the distribution of participations in an employee benefit plan to employees. The registration provisions of the 1933 Act apply only to the sale of securities and therefore the SEC interpretation effectively took noncontributory plans outside of the ambit of these provisions. *See, e.g., American Telephone and Telegraph Company* (SEC no-action letter available Nov. 8, 1976), *reprinted in* [1976-1977 Transfer Binder] FED. SEC. L. REP. (CCH) ¶80,870.

The SEC no-sale theory assumes either that participants give nothing of value for the securities or that the participants never consciously choose to acquire the securities. *See* SEC Brief, *supra* note 4, at 64. In its *Daniel* brief, the SEC generally repudiated both of these assumptions, noting that an employee gives value and makes an investment decision in deciding to accept employment or to remain employed. *Id.* at 64-89.

Despite its apparent change of position with respect to the no-sale theory, the SEC has issued no-action letters agreeing that no registration is required in situations where the no-sale theory would have previously been relied upon. *See, e.g., Norton Simon, Inc./Hunt-Wesson Foods, Inc.* (SEC no-action letter available June 8, 1978); *Texas Industries, Inc.* (SEC no-action letter available Feb. 16, 1979). For a more extensive discussion of the application of the no-sale theory, *see* Tomlinson, *supra* note 4, at 132-34.

Participation in contributory plans not permitting the use of participant contributions to purchase employer securities were also not required to be registered. *1978 ERISA Improvements Act Hearings, supra* note 13, at 333 (statement of Harold M. Williams, Chairman, SEC); *see 1968 House Hearings, supra* note 26, at 108 (statement of Davidson Sommers). It is not clear why this was so. It would appear that in all contributory plans the participant is purchasing an investment contract since the trustee will be investing his or her funds in securities. *See* Mundheim & Henderson, *Application of the Federal Securities Laws to Pension and Profit-Sharing Plans*, 29 LAW & CONTEMP. PROB. 795, 809 (1964) [hereinafter cited as Mundheim & Henderson]. Perhaps the SEC viewed the participant's contributions as the equivalent of direct purchases of the securities chosen by the trustee and, therefore, sales exempt by section 4(1) of the Securities Act. 15 U.S.C. §77(d)(1) (1976). Nevertheless, in a similar situation where the return also depended upon the investment policy of the fund manager, at least one justice found that investors are in need of 1933 Act disclosures. SEC v. Variable Annuity Life Ins. Co., 359 U.S. 65, 73 (1959) (Brennan, J., concurring); *see* Note, *supra* note 4, at 188-89. On the other hand, the granting of participations in contributory plans permitting the purchase of employer securities with participant contributions was regarded by the SEC as a public offering and sale of a security to participants. *See 1978 ERISA Improvements Act Hearings, supra* note 13, at 333 (statement of Harold M. Williams, Chairman, SEC). *See generally* SEC v. Ralston Purina, 346 U.S. 119 (1953). The SEC, therefore, required registration of the participations.

While the SEC's position on the matter is not wholly clear, it has in the recent past generally treated the employer as the issuer of the participations, rather than the trust. In 1965, the SEC noted that "a separate security [the participation] may be created which will be required to be registered under the Securities Act of 1933 and the issuer of which may be an investment company required to register under the Investment Company Act of 1940." SEC Release No. 33-4790 (July 13, 1965), *reprinted in* 1 FED. SEC. L. REP. (CCH) ¶1131. The reference to the Investment Company Act of 1940 permits an inference that the SEC did not expect that the issuer would be the employer. Furthermore, the Assistant General Counsel of the

position that there are two possible securities, the participant's interest in the plan [34] and the plan's interest in its own trust.[35]

The conclusion that there are two securities would lead one to expect the same application of section 3(a)(2) as that outlined in *Daniel.* Instead, the SEC has concluded that the interests and participations exempted by section 3(a)(2) include both the employees' interest in the plan and the plan's interest in its trust.[36] The SEC relies on the legislative history underlying the 1970 amendments to section 3(a)(2) to demonstrate that Congress intended to exempt both interests.[37] This is an abrupt change of position—eighteen months earlier, the SEC argued to the Supreme Court that the legislative history of section 3(a)(2) indicated that Congress intended to exempt a single security, the participant's interest in the benefit plan trust.[38]

IV. LEGISLATIVE HISTORY OF 1970 AMENDMENTS TO SECTION 3(a)(2)

Both the Supreme Court and the SEC rely on section 3(a)(2)'s legislative history to support their contrary positions. That history will now be examined.

SEC in an opinion published in 1941 noted that "the issuer of the investment contracts is frequently the trust", but gave no guidance as to what the distinguishing features were between situations in which the trust was the issuer and situations in which it was not. Opinion of Asst. General Counsel of Commission (1949), *reprinted in* [1941-1944 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 75,195.

The SEC requires that the registration form for participations, Form S-8, be completed by the employer. The Form S-8 instructions do not state that the employer is filing on behalf of the trust as issuer, but that "the term 'issuer' as used in this form means the person whose securities are to be offered pursuant to the [benefit] plan." General Instruction B to Form S-8. In a 1978 release announcing amendments to the Form S-8 signature requirements, the SEC noted that Form S-8 "requires, as do all registration forms, that the issuer sign the registration statement. In addition, unlike most other registration forms, it requires entities other than the issuer to sign the form. Specifically, it provides that the employee benefit plan must sign . . . ." SEC Release No. 33-5951 (July 28, 1978), *reprinted in* [1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 81,655. The release further states that the trustee of the trust holding the employee benefit assets need not sign the form. This seems rather clearly to suggest that SEC has identified the employer as the issuer of the participations.

34. The SEC defines "plan" to be "the permanent program or arrangement under which participating employees will become entitled to benefits." SEC Release No. 33-6188, *supra* note 3, at 84.

35. *Id.* at 80. The release indicates that the plan's interest may be in a single trust fund, collective trust fund or separate account. *Id.* This is not wholly accurate since bank collective trust funds qualified under the tax laws hold only the assets of pension plan trusts. *See* text accompanying notes 16-17 *supra.*

36. SEC Release No. 33-6188, *supra* note 3, at 8, 80, 87-90.

37. *Id.* at 87-89.

38. *See* note 70 *infra* and accompanying text.

The bulk of the amendments to section 3(a)(2) were introduced in two parts: the first in the Senate in 1967[39] and the second in the House of Representatives in 1970.[40] In 1967, Congress began consideration of a bill to clarify the status of bank-sponsored collective investment media under the Investment Company Act of 1940.[41] The bill as first introduced did not deal with section 3(a)(2) at all.

After initial hearings on the bill,[42] Senator McIntyre introduced an amendment (McIntyre Amendment) to the legislation which, among other things, ultimately amended section 3(a)(2) to exempt from the 1933 Act registration requirements interests in collective trusts maintained by banks for the investment of pension plan assets.[43] Banks had been sponsoring collective trusts which were made available to trustees of small pension plans for the investment of trust assets.[44] Trustees of these benefit plan trusts purchased interests in the large bank-sponsored collective trusts to achieve diversification and engage

39. Amendment No. 438 to S. 1659, 90th Cong., 1st Sess. § 102(b) (1967), *reprinted in Mutual Fund Legislation of 1967 Hearings on S. 1659 Before the Senate Comm. on Banking and Currency*, 90th Cong., 1st Sess. 1213 (1967) [hereinafter cited as McIntyre Amendment].

40. H.R. 17333, 91st Cong., 2d Sess. 116 CONG. REC. 13,494 (1970). The Teamsters' Brief to the Supreme Court in *Daniel* relies wholly on the history underlying the 1967 portion of the amendments and dismisses the 1970 portion as not affecting a basic congressional distinction between bank collective trusts and single trusts on the one hand and the plans creating the trusts on the other. Teamsters' Brief, *supra* note 4, at 121-29. The Supreme Court agreed with the Teamsters. *Compare* 439 U.S. at 565 n.19 *with* Teamsters' Brief, *supra* note 4, at 116, 118. Thus, if a plan issues a security, two securities exist, one issued by the trust and one by the plan.

The Seventh Circuit *Daniel* opinion, which adopted a position presented by the SEC (*compare* 561 F.2d at 1240-41 *with* SEC Seventh Circuit brief, *supra* note 26, at 30-34), and Plaintiff's Supreme Court brief (*see* Plaintiffs' Brief, *supra* note 4, at 72-78) point to the 1970 amendments as evidence of a congressional awareness that an employee's interest in a plan is a security and that this security is an interest in the plan trust. The SEC and plaintiff carried this argument too far in arguing that Congress also viewed all such interests to be securities notwithstanding the nature of the plan. The Supreme Court found this attempt to pull all interests in benefit plans within the definition of a security to be unwarranted. *See* note 26 *supra*. The Court took the argument as another example of an attempt by the SEC to extend the securities laws into areas not intended by Congress. 439 U.S. at 566 *citing* SEC v. Sloan, 436 U.S. 103, 117-19 (1978); Piper v. Chris-Craft Indus., Inc., 430 U.S. 1, 41 n.27 (1977); Ernst & Ernst v. Hochfelder, 425 U.S. 185, 212-14 (1976); United Housing Foundation, Inc. v. Forman, 421 U.S. 837, 858 n.25 (1975); Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 759 n.4 (1975) (Powell, J., concurring); Reliance Elec. Co. v. Emerson Elec. Co., 404 U.S. 418, 425-27 (1972).

41. S. 1659, 90th Cong., 1st Sess., 113 CONG. REC. 11255 (1967).

42. *1967 Senate Hearings, supra* note 13.

43. McIntyre Amendment, *supra* note 39, § 102(b).

44. *1967 Senate Hearings, supra* note 13, at 1283 (statement of Robert D. Ferguson); *1968 House Hearings, supra* note 26, at 27 (statement of Robert D. Ferguson); *1968 House Hearings, supra* note 26, at 84 (statement of John R. Haire); *Investment Company Amendments Act of 1969: Hearings on S. 34 and S. 296 Before the Senate Comm. on Banking and Currency*, 91st Cong., 1st Sess. 72 (1969) (statement of Reese H. Harris, Jr.) [hereinafter cited as *1969 Senate Hearings*]; *Mutual Fund Amendments: Hearings on H.R. 14737 Before the Senate Comm. on Commerce and Finance of the House Comm. on Interstate Commerce*, 91st Cong., 1st Sess. 463 (1969) (statement of Reese H. Harris, Jr.) [hereinafter cited as *1969 House Hearings*]; *see* Mundheim & Henderson, *supra* note 33, at 802.

investment management not generally available to the small pension plan trust.[45] Although interests in the bank's collective trust were arguably securities subject to the 1933 Act,[46] SEC administrative practice had long been not to require registration of interests in these trusts because they were not being offered to the public.[47] The McIntyre Amendment was intended to codify this administrative exemption for collective trusts.[48]

The small pension trusts were also subject to the 1933 Act and were also generally exempt by SEC administrative practice from registration of participations unless participant contributions were used to purchase employer securities.[49] But as the Teamsters pointed out to

45. *1967 Senate Hearings, supra* note 13, at 1283 (statement of Robert D. Ferguson); *1968 House Hearings, supra* note 26, at 27 (statement of Robert D. Ferguson); *1969 Senate Hearings, supra* note 44, at 72 (statement of Reese H. Harris, Jr.); *1969 House Hearings, supra* note 44, at 465 (statement of Reese H. Harris, Jr.).

46. *1967 Senate Hearings, supra* note 13, at 1273 (statement of Francis R. Schank); *1968 House Hearings, supra* note 26, at 52 (statement of Bruce McConnell, Jr.); *1968 House Hearings, supra* note 26, at 117 (SEC Memorandum of March 25, 1968).

47. *1967 Senate Hearings, supra* note 13, at 1284 (statement of Robert D. Ferguson); *1968 House Hearings, supra* note 26, at 27 (statement of Robert D. Ferguson); *id.* at 85 (statement of John R. Haire); *1969 Senate Hearings, supra* note 44, at 72 (statement of Reese H. Harris, Jr.); *1969 House Hearings, supra* note 44, at 465 (statement of Reese H. Harris, Jr.).

48. The amendment was necessary to preserve the SEC's administrative exemption for these trusts. There was some feeling that a failure to codify the administrative exemption for bank collective trusts would cast doubt upon its validity. *1967 Senate Hearings, supra* note 13, at 1284 (statement of Robert D. Ferguson); *1968 House Hearings, supra* note 26, at 27 (statement of Robert D. Ferguson); *1969 Senate Hearings, supra* note 44, at 72 (statement of Reese H. Harris, Jr.); *1969 Senate Hearings, supra* note 44, at 463 (statement of Reese H. Harris, Jr.).

49. *1967 Senate Hearings, supra* note 13, at 1326 (statement of Manuel F. Cohen, Chairman, SEC). Chairman Cohen stated:

> With respect to bank collective funds for tax exempt pension, profit-sharing, or retirement plans . . . the proposed amendments would provide exemptions from registration under the Securities Act of 1933. . . . The application of the Securities Act of 1933 to pension and welfare plans has presented difficulties over the years. Such plans could be regarded as involving the public offering of securities requiring registration . . . . [T]he Commission has not heretofore required registration of such plans . . . except where such plans are funded by investment in the employer's securities.

Id. at 1341-42 (Memorandum of the Securities and Exchange Commission).

Chairman Cohen's statement appears to confuse the pension plans with the bank collective funds in which the pension plan trusts were investing. Plans permitting funding with employer stock almost certainly were not investing their assets wholly in collective funds, since the bank's fiduciary duties with respect to diversification would almost certainly prohibit any significant investment in any employer's stock. In addition, some large pension plan trusts did not invest in bank collective media at all, but were still exempt under the SEC's administrative policy. The pension plan trusts are all deemed single trust funds for purposes of the 1933 Act despite the fact that in a contributory plan they represent the collective investment of participant's contributions. They are "single" because they hold all of the funds of one plan. The collective trusts referred to in section 3(a)(2) and the McIntyre Amendment are the trusts holding the funds of more than one plan. Thus, when Chairman Cohen was speaking of exemptions for pension plans, he was referring to exemptions for single trusts and not for collective trusts. Either Chairman Cohen misinterpreted the scope of the McIntyre Amendment or he was using the word "plan" as a shorthand reference for both the single trust and the

the Supreme Court, the McIntyre Amendment did not exempt interests in the benefit plan trusts from registration.[50] However, the House subsequently added language to the bill further amending section 3(a)(2)[51] to deal with interests in benefit plan trusts. Although the Teamsters[52] and the Court[53] construed this additional language as having little substantive impact, the SEC argued that this language exempted participant interests in benefit plan trusts.[54] Therefore, an understanding of the House amendment is crucial to the proper application of section 3(a)(2).

After passing the Senate in the Ninety-first Congress, the bill amending section 3(a)(2) was brought before the Subcommittee on Commerce and Finance of the House Committee on Interstate and Foreign Commerce. The Subcommittee held hearings[55] during which it received a letter from the General Counsel of Sperry Rand suggesting that since Congress was codifying SEC practice by exempting

collective trust. Chairman Cohen similarly confused interests in plans/single trust funds and collective trust funds when testifying before the House. *1968 House Hearings, supra* note 26, at 133, 141 (statement of Manuel F. Cohen, Chairman, SEC). This confusion between exempting bank collective trust funds and single trust funds establised under individual plans was not confined to the SEC. *See 1967 Senate Hearings, supra* note 13, at 1259 (Supplemental Memorandum of the Investment Company Institute).

The SEC later clarified the Chairman's testimony by submitting a memorandum which noted:

> In testimony before the Senate Committee, the Chairman expressed reservations about the proposed amendment insofar as it would provide an exemption for corporate pension plans which invest in the employer's stock . . . . [O]fferings of a company's securities . . . to employees are not uncommon . . . . [T]he Commission has found no justification for permitting avoidance of registration for such offerings . . . . The Commission, however, does not believe it is necessary to recommend changes in the proposed amendments to deal with employer plans which invest in the employer's stock, since the language of the amendment clearly indicates that it would exempt from registration only interests in the collective funds for corporate pension plans and not interests in the plans themselves. Thus, the legislation will not affect the Commission's existing authority to require Securities Act registration for interests in corporate pension plans which are funded by bank collective funds, even though interests in the funds are exempt from registration. The Commission could therefore require registration of plans in appropriate situations such as where the plans invest substantially in the employer's stock.

1967 Senate Hearings, supra note 13, at 1341-42.

50. Teamsters' Brief, *supra* note 4, at 121-25; *see 1967 Senate Hearings, supra* note 13, at 1220 (SEC Section by Section Analysis of Amendments to S. 1659 Proposed as Title II of the Investment Company Act Amendments of 1967); *1969 Senate Hearings, supra* note 44, at 42 (statement of Paul W. Eggers); S. REP. No. 184, 91st Cong., 1st Sess. 27 (1969).

51. *See* H.R. 17333, 27(b), 91st Cong., 2d Sess.; 116 CONG. REC. 13494 (1970).

52. Teamsters' Brief, *supra* note 4, at 125-30.

53. 439 U.S. at 565 n.19. The Supreme Court cited S. REP. No. 184, 91st Cong., 1st Sess. 27 (1969), and the *1967 Senate Hearings, supra* note 13, at 1341-42 (Memorandum of SEC), relating to the McIntyre Amendment.

54. SEC Seventh Circuit Brief, *supra* note 26, at 30-34.

55. *1969 House Hearings, supra* note 44.

interests in bank-maintained collective trusts from the 1933 Act, it ought also to codify SEC practice with respect to pension plan trusts by exempting them from the 1933 Act as well.[56] Apparently in response to this suggestion, the Subcommittee amended the legislation to exempt "any interests . . . in a single . . . trust fund . . . ."[57]

56. Letter from Stannard Dunn, General Counsel, Sperry Rand Corp., to John E. Moss, Chairman, Subcomm. on Commerce and Finance of the House Comm. on Interstate and Foreign Commerce (November 7, 1969), *reprinted in 1969 House Hearings, supra* note 44, at 929-30. Mr. Dunn wrote:

> We would like to suggest . . . an amendment [to] clarify the registration provisions of the Securities Act of 1933 by codifying a long established administrative practice of the [SEC] . . . . [The present bill] would . . . exempt from Securities Act registration any interests or participations in any "common" or "collective" trust fund . . . . [It] does not appear to exempt interests or participations in . . . a plan under which funds are paid to a bank trustee that invests them in its discretion (without commingling with other trust funds in a "common" or "collective" trust fund) . . . .
>
> The staff of the Securities and Exchange Commission has for some time . . . advised companies that it would not recommend that the Commission take action if the company offered to its employees, without registration under the Securities Act of 1933, interests or participations in a plan if no portion of the fund attributable to employees' contributions were invested in the employer's own securities. Such advice . . . does not purport to exempt the interests or participations from any registration requirement nor to afford legal protection against civil suits under the Securities Act or actions under state "blue sky" laws. Obviously, this has not been a satisfactory treatment of the problem.
>
> We think that the Securities and Exchange Commission reached this same conclusion, because two years ago it recommended a clarifying amendment to the Securities Act. You will recall that in 1967 the Subcommittee on Commerce and Finance of the Committee on Interstate and Foreign Commerce held hearings on bills that would have amended Section 3(a)(2) of the Securities Act in a manner similar to the amendments proposed by the current bills. The Commission then recommended the addition to those bills of an exemption for "any employees" stock bonus, pension or profit-sharing trust which meets the requirements of Section 401 of the Internal Revenue Code (citation omitted).

Mr. Dunn appears to have misinterpreted the SEC's earlier suggestion which was made during the House's 1968 hearings on a bill substantially the same as the McIntyre Amendment. *1968 House Hearings, supra* note 26, at 118, 121. The SEC's proposed amendment dealt only with bank collective trusts holding assets of more than one tax qualified pension plan. *Id.* at 114, 118 (SEC Memorandum with Respect to Changes in the Provisions of H.R. 14742 Dealing with Bank Collective Investment Funds, March 25, 1968). The language proposed by the SEC to which Mr. Dunn refers would have exempted from registration "any interest or participation in any common trust fund . . . maintained by a bank exclusively for the collective investment . . . of assets contributed thereto by . . . any employees' stock bonus, pension, or profit-sharing trust . . . ." *Id.* at 121. While the SEC's language was somewhat inartful and subject to the interpretation suggested by Mr. Dunn, the context makes it relatively clear that it was intended to read as edited above.

57. H.R. 17333, 91st Cong., 2d Sess. §27(b), 116 CONG. REC. 13494 (1970). The SEC has opined that the trustee of a single trust need not be a bank to qualify for a section 3(a)(2) exemption. SEC Release No. 33-6188, *supra* note 3, at 91-92; *Communications Workers of America* (SEC no-action letter available January 27, 1980), *reprinted in* [Current Transfer Binder] FED. SEC. L. REP. (CCH) ¶76,321; *Norton Simon, Inc. and Glass Containers Corporation* (SEC no-action letter available November 16, 1979); *New England Electric System Companies Pension Plan* (SEC no-action letter available May 7, 1979); *Gilbert Associates, Inc.* (SEC no-action letter available Dec. 1, 1977), *reprinted in* [1977-1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶81,406. Congress has now amended §3(a)(2) to make this explicit. *See* note 14 *supra*.

Unfortunately, it is not clear that this language is actually in response to the Sperry Rand letter.[58] The House Report ignores the additional exemption for single trust funds entirely. It reported only that the amendments to section 3(a)(2)

> exempt from the registration provisions of the act interests or participations in collective trust funds maintained by banks for funding certain stock-bonus, pension or profit-sharing plans . . . . In effect, the amendment would exempt interests or participations in connection with corporate pension or profit-sharing plans . . . . The exemption is limited to interests or participations in those bank collective trust funds maintained for the funding of employers' stock bonus, pension, or profit-sharing plans and not as vehicles for direct investment by individual members of the public.[59]

Nevertheless, the debate in the House on the amended bill indicates clearly that the additional exemption for single trusts was intended to reach employee interests in pension plan trusts:

> MR. SPRINGER. . . . Section 27(b) of the bill provides an exemption from registration under the Securities Act of 1933 for interests or participations in trust funds maintained by banks for funding certain stock bonus, pension or profit-sharing plans. . . . I understand that this bill differs slightly from the bill passed by the Senate in that it would make it clear that interests in a single trust maintained by a bank where the trust assets were not commingled with those of other qualified trusts would also be exempted from the registration requirements of the Securities Act. I understand that the SEC has required registration of interests and participations in such trust funds where employee money is used to buy securities of the employer . . . . I understand that this bill would not prevent the SEC from requiring registration of interests or participation in such trusts if that also were the case. Am I correct?
>
> MR. MOSS. The gentleman is correct. It is my understanding that that is what was intended.[60]

58. *Compare* Teamsters' Brief, *supra* note 4, at 127 n.114 *and* Latto, *supra* note 32, at 743, *with* Plaintiff's Brief, *supra* note 4, at 75-77.

59. H.R. REP. No. 1382, 91st Cong., 2d Sess. 43 (1970). The Teamsters cited this absence as proof of the lack of significance ascribed to the additional language. *See* Teamsters' Brief, *supra* note 4, at 126.

60. 116 CONG. REC. 33287 (1970). The Teamsters' Brief cites this colloquy for the proposition that Congress distinguished between pension plans and the trusts established under those plans. Teamsters' Brief, *supra* note 4, at 126, 172. Thus, the Teamsters argued:

> This deliberate and authoritative colloquy far from stating that there had been a significant change in "focus," declared that the House bill differed from the Senate bill "slightly," in that a single trust maintained by a bank where the trust assets were *not* commingled with those of other qualified

In addition, the House Conference Report stated that the "House amendment . . . codified a long established administrative practice of the Commission by making it clear that the exemption applied not only to collective trust funds, but also to single trust funds." [61] Oddly, given the colloquy on the House floor, the legislation did not permit the SEC to require registration of contributory plans investing in employer securities.[62] But the Conference Committee amended the legislation to conform to SEC practice by excluding from the exemption interests in plans permitting the use of participant contributions to purchase employer securities.[63] Finally, because the interests in a single trust are themselves arguably employer securities,[64] an exclusionary parenthetical was added to section 3(a)(2) which read as follows: "(other than interests or participations in the trust . . .)". This parenthetical addition was made by attaching a rider to a subsequent bill.[65]

V. RESOLUTION: ONE SECURITY OR TWO?

From the foregoing it seems reasonable to conclude that the House amendment was intended to codify SEC policy exempting from registration securities issued by benefit plan trusts not permitting the purchase of employer securities with participant contributions.[66] It

trusts would *also* be exempted from registration under the securities laws; that is, they would be treated like "collective trusts maintained by a bank" under the Senate bill.

Id. at 127.

The Teamsters went to much effort to distinguish an interest in the plan from an interest in the trust and therefore argued that Congress distinguished between the plan and its trust. *See id.* at 126. *See generally* Latto, *supra* note 32, at 737-44. Nevertheless, the Teamsters never adequately dealt with the consequence of such a distinction in the context of a single trust fund. *See* notes 61-66, *infra*, and accompanying text. If, as is likely, Congress did not distinguish between the pension plan and its trust, then the colloquy is significant evidence that section 3(a)(2) was intended to exempt participations in defined contribution plans.

The Teamsters did not need to argue that section 3(a)(2) embodied a Congressional distinction between pension plans and underlying trusts. If, as the Court ultimately held, interests in defined benefit plans are not securities in part because participants do not have an interest in the trust, then section 3(a)(2) was never applicable to plans like that in *Daniel*. Section 3(a)(2) is applicable to plans where the employee is being offered an interest in the trust and it is precisely those plans that Congress had in mind when exempting single trusts. *See* note 26 *supra*.

61. H.R. CONF. REP. No. 1631, 91st Cong., 2d Sess. 31 (1970).

62. 116 CONG. REC. 33295 (1970).

63. H.R. CONF. REP. No. 1631, 91st Cong., 2d Sess. 24 (1970).

64. *See* 561 F.2d at 1241; SEC Seventh Circuit Brief, *supra* note 26, at 34; note 39 *supra*.

65. S. 3431, 91st Cong., 2d Sess., Pub. L. No. 91-567, sec. 6(a), § 3(a)(2), 84 Stat. 1497 (1970).

66. *See* Latto, *supra* note 32, at 749. Congress itself appears to have interpreted the statute in this matter. A study initiated by a Senate subcommittee reported that "[p]ension and profit-sharing plans are exempt from coverage under the Securities Act of 1933 . . . unless the plan is a voluntary contributory pension plan and invests

is important that this policy did not create a distinction between interests in the benefit plan trust and participations in the plan.[67] From the 1940's through the mid-1960's, the SEC apparently believed that the participations were issued by the benefit plan trust.[68] More recently, however, its position has been that participations are issued by the employer.[69] This position explains the need for the belated parenthetical addition to section 3(a)(2). But in either event the SEC had never found more than one security representing an interest in the plan/trust.[70] Thus, the legislative history of section 3(a)(2) and the administrative practice preceding the 1970 amendments to the Section establish that a participation in a plan is an interest in the trust and that Congress did not independently identify two securities. Nevertheless, the Supreme Court in *Daniel* found Congress to have done exactly that.

The Supreme Court flatly rejected the SEC's analysis of the exemption for single trusts and the need for the additional parenthetical. Instead the Court noted:

> The SEC argues that the addition by the House of the language "single or" before "common trust fund" indicated an intent to cover the underlying plans that invested in bank maintained funds. The legislative history, however, indicates that the change was meant only to eliminate the negative inference suggested by the unrevised language that banks would have to register the segregated investment funds they administer for particular plans. Because the provision as a whole dealt only with the relationship between a plan and its bank, the revision did not affect the registration status of the underlying plan. See 116 Cong. Rec. 33287 (1970) [quoted in relevant part at text accompanying note 60 *supra*]. This was consistent with the SEC's interpretation of the provision. [1967 Senate] Hearings, *supra* [note 13], at 1326 [quoted in relevant part at note 49 *supra*]. The subsequent addition of another provision ex-

in the securities of the employer company in an amount greater than that paid into the plan by the employer." S. REP. No. 634, 92d Cong., 2d Sess. 96 (1972); *see* 126 CONG. REC. S13465 (daily ed.) Sept. 25, 1980).

67. Mundheim & Henderson, *supra* note 33, at 801-02, 810. "Perhaps because of its concentration on the investment company nature of trusteed plans, Commission statements concerning them do not distinguish between the plan and the trust which is used to fund it." *Id.* at 802 n.21.

68. *See* note 33 *supra*.

69. *Id.*

70. *See* SEC Brief, *supra* note 4, at 61 n.48. The SEC noted:

> In the case of a single pension fund, there is only one security—the employee's interest in that fund. A bank or insurance company may have investment discretion over the assets of a single fund, but it is not considered to have sold that fund a security separate from the employee's interest in the fund.

Id. *But see* Latto, *supra* note 32, at 739.

> cepting from the exemption funds "under which an amount in excess of the employer's contribution is allocated to the purchase of securities . . . issued by the employer or by any company directly or indirectly controlling, controlled by or under common control with the employer" appears to have been simply an additional safeguard to confirm the SEC's authority to require such plans, and only such plans, to register. See H.R. Conf. Rep. No. 91-1631, p. 31 (1970) [quoted in relevant part *supra* at text accompanying note 59].[71]

If, as the Court asumes, two separate securities are issued—the interest issued by the benefit plan trust and the participation issued by the plan or employer—and if section 3(a)(2) applies only to the former, then Congress has created a most curious exemption. It has exempted the sale by the benefit plan trust of 100% of the interest in the trust to the entity which both created the trust and determined its investment policies.[72] Almost assuredly such a sale, if it exists at all,[73] would already be exempt by section 4(2) of the 1933 Act as an issuer transaction not involving a public offering.[74] In addition, if two securities with different issuers exist, what possible need could there be for the parenthetical addition to the statute? While Congress apparently felt strongly enough about the parenthetical to add it as a rider to subsequent legislation,[75] the Supreme Court's interpretation would have it be mere surplusage.

Furthermore, under the Court's construction, it is impossible to see why trusts established under noncontributory plans should be exempt while trusts established under some contributory plans are not. The entity establishing the trust has no more need for disclosure in one instance than the other.[76] The employees have a greater need for

71. 439 U.S. at 565 n.19.

72. *See* text accompanying notes 15-17 *supra*. As the SEC noted in its brief:

> It is unrealistic to assert that the pension fund is itself holding a security consisting of a trust containing solely the pension fund's own assets. Accordingly, if section 3(a)(2) did not apply to the employee's interest . . . there would be nothing, in the case of single funds, to be exempted by the section and Congress' exemption of interests in single funds would serve no purpose.

SEC Brief, *supra* note 4, at 61 n.48.

73. In such an instance it seems likely that the bank is no more than an agent for the plan and that no sale takes place at all.

74. 15 U.S.C. § 77d(2) (1976).

75. S. 3431, 91st Cong., 2d Sess., Pub. L. No. 91-567, sec. 6(a), § 3(a)(2), 84 Stat. 1497 (1970).

76. There was discussion concerning plan trustees' need for 1933 Act disclosures from the bank trustee during the hearings on the 1970 amendments to section 3(a)(2). *See 1967 Senate Hearings, supra* note 13, at 1259 (Supplemental Memorandum of Investment Company Institute); *1968 House Hearings, supra* note 26, at 118 (SEC Memorandum of March 25, 1968). The Investment Company Institute Memorandum stated:

> [T]hese collective funds may be utilized by thousands of small corporations for their pension funds. If large banks . . . actively market and promote

disclosure in one case than the other, but the plan trustees are in virtually identical positions vis-à-vis the bank in both types of plans.[77]

In sum, the Court's interpretation of section 3(a)(2) has Congress creating an exemption for a security not before known to exist, the sale of which was already exempt. Surely, Congress did not undertake such a pointless exercise.[78]

The SEC in its post-*Daniel* release avoided the logical inconsistencies of the *Daniel* two securities analysis by interpreting section 3(a)(2) to apply to both.[79] The SEC's analysis of why section 3(a)(2) applies to both securities is instructive:

> The legislative history of the 1970 Amendments indicates that their original purpose was to alleviate a concern expressed by banks and insurance companies that there was no clear exemption from registration in the 1933 Act for interests in the collective funding vehicles maintained by those entities for employee benefit plans. While the amendments were under consideration, however, language was added that reflected the Commission's consistent administrative practice of not requiring interests in plans to be registered except where employee money is used to buy securities of the employer.
>
> . . . [T]he implicit purpose of the 1970 Amendments was to exempt not only the interests of plans in certain investment vehicles, but also the interests of participants in the plans themselves. This position is reasonable when one considers that, from the employee's standpoint, his interest in the plan is inseparable from his aliquot share of the plan's interest in the funding vehicle. Moreover, there is the practical consideration that if Section 3(a)(2) were not broadly construed to cover employee interests in plans as well as plan interests in funding vehicles, many plans would have no exemption from registration upon which to rely for the offer and sale of interests to employees. Accordingly, the staff believes it is appropriate to link both the plan's interest in a funding vehicle and the interests of participants in the plan itself for purpose of the exemption provided by Section 3(a)(2).[80]

Thus, the SEC asserts that the participant's interest in the plan is indivisibly "linked" to the plan's interest in its trust and it would be

interests in these funds as part of their pension fund business, there is no good reason why these small businesses should not have at least the disclosure protection of the 1933 Act.

See also Mundheim & Henderson, *supra* note 33, at 802.

77. *See* notes 30-32 *supra* and accompanying text.

78. *See* note 26 *supra*.

79. SEC Release No. 33-6188, *supra* note 3, at 8, 87-90.

80. *Id.* at 87-89 (citations omitted).

senseless to exempt one interest but not the other. In substance, this position is identical to the argument for the proposition that the two interests are indivisible because there is only one interest.

The SEC has accepted the Supreme Court's finding of two securities but has rejected the Court's application of section 3(a)(2) to only one of the two interests. Yet, if there are two possible securities, then the Court seems justified in construing section 3(a)(2) to apply to only one. A solution to the dilemma is to acknowledge that Congress found only one security and then only in the context of defined contribution plans.[81] It then drafted section 3(a)(2) to exempt that security from the registration provisions of the Securities Act. Therefore, as the SEC suggests in its post-*Daniel* release, section 3(a)(2) exempts employee interests in all employee benefit plans which are qualified under section 401 of the Internal Revenue Code and which do not both place contributions in a single trust and permit employee contributions to be used to purchase employer stock.

VI. CONCLUSION

Daniel was a case poorly suited for a judicial construction of section 3(a)(2). The parties and *amici* argued section 3(a)(2)'s legislative history in an attempt to prove a proposition unrelated to the section itself. In so doing they presented the Supreme Court with limited views of congressional purpose in enacting the section 3(a)(2) exemptions.

The Court, sensing that the SEC had pushed the 1933 Act further than Congress intended it to go, reacted by adopting the other, contrary, position presented to it. It is unfortunate that the Court did not follow the Chief Justice's suggestion to leave construction of section 3(a)(2) for another case where an interpretation was genuinely necessary.[82] By adopting the Teamsters position, the Court reached a strained construction of the statute which requires a congressional intent not in evidence, and which does not comport with SEC or securities bar practice either before or after the 1970 amendments to section 3(a)(2). If the Court's interpretation is put into practice, many employers and trustees may be found to be in violation of the 1933 Act because they have sold unregistered securities.[83] Such

81. *But see id. at* 23-25.

82. 439 U.S. at 570 (Burger, C.J., concurring).

83. The distinction between one security and two is not very important under the 1933 Act if section 3(a)(2) applies to all interests in the plan and trust. However, in instances where section 3(a)(2) does not exempt the benefit plan related securities, a new issuer—the plan's trust—has been created, and presumably the trust must register the interest sold to the plan. Furthermore, a two security

a result would advance neither congressional purposes underlying the securities acts nor the legislation authorizing and regulating the affected employee benefit plans.[84]

The SEC, however, has not followed the Court's interpretation of section 3(a)(2) [85] and employers and trustees have thus far followed the SEC's lead by not registering interests in their plans. It is to be hoped that the first court actually confronted with the task of construing section 3(a)(2) in a case where section 3(a)(2) is at issue will thoroughly examine the relevant legislative history and not follow the Supreme Court's interpretation in *Daniel*.[86]

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analysis would create a new transaction, the sale of the trust interest to the plan, to which the antifraud provisions of the federal securities laws would apply, and which might then lead to further litigation like *Daniel*. Lastly, the registration and antifraud provisions of the Blue Sky laws of the states would be applicable. This multiplicity of regulation serves only to make plans more costly to implement and, therefore, less attractive to employers. The loser in the long run is the employee.

Like the staff position in SEC Release No. 33-6188, note 3 *supra*, at 87-90, the theory that only one security exists conflicts with the dicta in *Daniel*. Nevertheless, the single security analysis finds ample support in the legislative history and the SEC's own past practice.

84. Tomlinson, *supra* note 4, at 123-25.

85. *1979 ERISA Improvements Act Hearings*, *supra* note 26, at 701-02 (Report of the Staff of the Securities and Exchange Commission).

86. *But see id.* at 747. One court has already construed section 3(a)(2) as suggested in this article but did not comment on the *Daniel* interpretation of the statute. Leonard v. Drug Fair, Inc., [1979-1980 Transfer Binder] FED. SEC. L. REP. (CCH) ¶97,144 (D.D.C. 1979).