

REVENUE RULE 94-76

1994-2 C.B. 46, 1994-50 I.R.B. 5.

**Internal Revenue Service
Revenue Ruling**

TRANSFERS; ROLLOVERS; PROTECTED BENEFITS

November 29, 1994

Sec. 401. Qualified Pension, Profit-sharing And Stock Bonus Plans, 26 CFR 1.401-1: Qualified pension, profit-sharing and stock bonus plans.

Transfers; rollovers; protected benefits. Whether, in specified circumstances, changes in plan provisions governing amount transferred or directly rolled over from a qualified money purchase pension plan to an otherwise qualified profit-sharing plan will cause the profit-sharing plan to fail to satisfy the requirements of section 401(a) of the Code.

ISSUE

Whether, in the situations described below, changes in the plan provisions governing amounts transferred (Situation 1) or directly rolled over (Situation 2) from a qualified money purchase pension plan to an otherwise qualified profit-sharing plan will cause the profit-sharing plan to fail to satisfy the requirements of s 401(a) of the Internal Revenue Code.

FACTS

Situation 1: Employer X maintains a money purchase pension plan ("Plan A") that is qualified under s 401(a). Plan A provides that distribution of accrued benefits may be made to employees only upon retirement, death, disability, severance of employment, and termination of the plan. Plan A covers all of the employees of X. Plan A does not permit voluntary employee contributions. The employees of X are organized into 2 divisions, Division 1 and Division 2. In 1994, X establishes a discretionary profit-sharing plan ("Plan B") for the benefit of employees in Division 2 only. Plan B provides for all of the optional forms of benefit provided under Plan A, including the joint and survivor annuity option. However, unlike Plan A, Plan B also permits employees to elect to receive a distribution of any portion of their nonforfeitable accrued benefit after the amount has been in the employee's account for at least two years.

X amends Plan A and Plan B to provide that the Plan A assets and liabilities of the employees of Division 2 will be transferred from Plan A to Plan B in a spinoff of Plan A and merger with Plan B that satisfies the requirements of s 414(l). The provisions of Plan B, including its distribution provisions, remain in effect without modification after the transfer, and apply to the assets and

liabilities transferred from Plan A. All applicable notice requirements are satisfied with respect to the transfer.

Situation 2: Employer Y maintains a money purchase pension plan ("Plan C") that is qualified under s 401(a). Plan C provides that distribution of accrued benefits may be made to employees only upon retirement, death, disability, severance of employment, and termination of the plan. In 1994, Y terminates Plan C and establishes a profit-sharing plan ("Plan D"). Plan D permits employees to elect, at any time, a distribution of accrued benefits that are attributable to any amount rolled over to Plan D.

Upon termination, Plan C is amended to provide employees the additional distribution option of electing an immediate single-sum distribution equal to the employee's account balance. If an employee elects distribution in a single sum, the employee may also elect to have the distribution paid to Plan D in a direct rollover to the extent the distribution is an eligible rollover distribution.

Employee S elects a single-sum distribution consisting of S's entire account balance from Plan C and elects to have the distribution paid directly to Plan D in a direct rollover that satisfies the requirements of s 401(a) (31). The applicable requirements of §§ 411(a) (11) and 417 and the notice requirements of s 402(f) are satisfied with respect to the distribution before it is paid in a direct rollover.

LAW

Section 401(a) provides that a trust created or organized in the United States and forming a part of a qualified stock bonus, pension, or profit-sharing plan of an employer constitutes a qualified trust only if the various requirements set out in s 401(a) are met.

Section 1.401-1(b) (1) (i) of the Income Tax Regulations provides the definition of a pension plan. This section provides, in part, that a pension plan is a plan established and maintained by an employer primarily to provide for the payment of definitely determinable benefits to employees over a period of years, usually for life, after retirement. This section also provides that a pension plan may provide for the payment of a pension due to disability, and may also provide for incidental death benefits.

Rev. Rul. 56-693, 1956-2 C.B. 282, as modified by Rev. Rul. 60-323, 1960-2 C.B. 148, provides that a pension plan fails to meet the requirements of s 401(a) if it permits an employee to withdraw any part of the employee's accrued benefit (other than a benefit attributable to voluntary employee contributions) prior to certain distributable events; e.g., retirement, death, disability, severance of employment, or termination of the plan.

Section 1.401-1(b) (1) (ii) provides the definition of a profit-sharing plan. This section provides, in part, that a profit-sharing plan is a plan established and maintained by an employer to provide for the participation in its profits by its employees. This section also

provides that a profit-sharing plan may provide for the distribution of funds accumulated under the plan after a fixed number of years.

Rev. Rul. 71-295, 1971-2 C.B. 184, provides that the term "fixed number of years" as used in s 1.401-1(b) (1) (ii) is considered to mean at least two years.

Section 401(a) (31) requires a qualified plan to permit a distributee of any eligible rollover distribution to elect (in such form and at such time as the plan administrator may prescribe) to have the distribution paid directly to an eligible retirement plan as a direct rollover.

Section 1.401(a) (31)-1T, Q&A-14 provides that for purposes of applying the qualification requirements of s 401(a), a direct rollover is a distribution and rollover of the eligible rollover distribution and not a transfer of assets and liabilities.

Section 402(c) (8) (B) defines an eligible retirement plan to include a qualified trust under s 401(a).

Section 402(c) defines an eligible rollover distribution as the taxable portion of any distribution to an employee of all or any portion of the balance to the credit of the employee in a qualified trust except for minimum distributions required under s 401(a) (9) and certain periodic annuities.

Section 414(l) provides, in part, that a plan will not qualify under s 401(a), in the case of any transfer of assets or liabilities of such plan to any other plan, unless each employee in the plan would (if the plan then terminated) receive a benefit immediately after the transfer that is equal to or greater than the benefit the employee would have been entitled to receive immediately before the transfer (if the plan had then terminated).

Section 1.414(l)-1(o) provides that any transfer of assets or liabilities will, for purposes of s 414(l), be considered as a combination of spinoffs and mergers.

Section 1.414(l)-1(b) (4) defines a spinoff as the splitting of a single plan into two or more plans.

Section 1.414(l)-1(b) (2) defines a merger as the combining of two or more plans into a single plan.

Section 411(d) (6) (A) provides that a plan will not be a qualified plan if an employee's accrued benefit is decreased by any amendment of the plan (with exceptions not here relevant).

Section 411(d) (6) (B) provides that a plan amendment that has the effect of eliminating an optional form of benefit with respect to benefits attributable to service before the amendment is treated as reducing accrued benefits.

Section 1.411(d)-4, Q&A-2(b) provides that the Commissioner may provide that certain plan amendments that otherwise would be treated as not satisfying s 411 because of s 411(d)(6) will satisfy s 411(d)(6) to the extent the amendments are necessary to enable a plan to comply with other requirements of s 401(a).

ANALYSIS

Situation 1: Under s 414(l), the transfer of certain assets and liabilities from Plan A to Plan B is considered a spinoff of those assets and liabilities from Plan A and the merger of those assets and liabilities with the assets and liabilities of Plan B. The merged entity consists of both the assets and liabilities transferred from Plan A and the assets and liabilities of Plan B. A merger of assets and liabilities of a qualified money purchase pension plan with the assets and liabilities of a qualified profit-sharing plan does not divest the assets and liabilities of the money purchase pension plan of their attributes as pension plan assets and liabilities. Therefore, to satisfy s 401(a), the assets and liabilities transferred from Plan A to Plan B must remain subject to the restrictions on distributions applicable to a qualified money purchase pension plan. In order to remain qualified, any plan provision applicable to the accrued benefits derived from Plan A must not permit distributions prior to retirement, death, disability, severance of employment, or termination of the plan. Plan B's distribution provisions permit distribution of an employee's accrued benefit after two years. The application of these distribution provisions to the accrued benefits transferred from Plan A therefore causes the merged plan to fail to satisfy s 401(a).

In order for Plan B to remain qualified, Plan B must be amended to provide that on and after the transfer, the accrued benefits attributable to the assets and liabilities transferred from Plan A to Plan B (i.e., the account balances including the post-transfer earnings thereon) will be distributable only on or after events that are permissible under qualified pension plans. In order to avoid a violation of the provisions of s 411(d)(6), the amendment to Plan B must be adopted on or before the date of the transfer from Plan A to Plan B. This is because the right to take a distribution of an employee's accrued benefit after two years is an optional form of benefit. Accordingly, if Plan B were amended to eliminate that right with respect to benefits that have accrued, that amendment would be eliminating a s 411(d)(6) protected benefit. See s 1.411(d)-4, Q&A-1, 2. Furthermore, in order to implement the Plan B amendment that imposes the pension plan distribution restrictions on the Plan B assets and liabilities that were transferred from Plan A to Plan B and not on the other Plan B assets and liabilities, there must be an acceptable separate accounting between the accrued benefits attributable to the transferred assets and liabilities and all other benefits under Plan B. See, s 1.401(a)-20, Q&A- 5(b) for a description of an acceptable method of separate accounting.

The result in this revenue ruling will be the same whether or not the transfer in situation 1 constitutes a partial termination under s 411(d)(3). In addition, the result in this revenue ruling would be the same if, instead of transferring the assets and liabilities of all of the employees of Division 2 from Plan A to Plan B, Employer X had

transferred from Plan A to Plan B the assets and liabilities of some, but not all, of the employees in Division 2. Similarly, the result in this revenue ruling would not differ if, instead of transferring only some of the assets and liabilities of Plan A from Plan A to Plan B, Employer X had merged Plan A with Plan B and extended Plan B's distribution provisions to the accrued benefits under the merged plan that were attributable to benefits from Plan A. Furthermore, the result in this revenue ruling would not differ if Plan B had been a stock bonus plan, instead of a profit-sharing plan.

Situation 2: Pursuant to Q&A-14 of s 1.401(a)(31)-1T, for purposes of applying the qualification requirements of s 401(a), the direct rollover of the entire amount of Employee S's account balance to Plan D is a distribution and rollover of the amount and not a transfer of assets and liabilities under s 414(l). Once assets are properly distributed from a qualified plan in accordance with its terms, the liabilities of the plan with respect to the distributed plan assets are discharged and the amounts distributed are no longer assets of a qualified plan. Therefore, in order to remain qualified, an eligible retirement plan is not required to provide, with respect to amounts paid to it in a direct rollover, the same optional forms of benefit that were provided under the plan that made the direct rollover. In addition, the application of the immediate distribution provisions of Plan D to benefits attributable to rollover contributions does not cause Plan D to fail to satisfy the requirements of s 401(a) on or after the date Plan D accepts a rollover contribution in the form of a distribution paid in a direct rollover by Plan C.

HOLDINGS

Situation 1: The provision of Plan B that permits employees to elect a distribution of any amount of an employee's nonforfeitable accrued benefit, including benefits transferred from Plan A, to be made after the amount has been in the employee's account for at least two years will cause Plan B to fail to satisfy the requirements of s 401(a).

Situation 2: The provision of Plan D that permits employees to elect a distribution of accrued benefits that are attributable to rollover contributions from a qualified plan (including benefits from Plan C that are received in a direct rollover) does not cause Plan D to fail to satisfy the requirements of s 401(a).

CORRECTIVE PLAN AMENDMENTS

Pursuant to the authority contained in s 1.411(d)-4, Q&A-2(b), the Commissioner has determined that a profit-sharing plan or stock bonus plan is permitted to be amended to eliminate an optional form of benefit provided for in the plan on or before December 12, 1994, solely with respect to benefits attributable to assets and liabilities (other than any portion of those assets and liabilities attributable to voluntary employee contributions) that are transferred within the meaning of s 414(l) from a money purchase pension plan (i.e., the transferred money purchase plan account balances including the post-transfer earnings thereon), to the extent that the optional form permits distribution of those benefits prior to the employee's

retirement, death, disability, or severance from employment, or plan termination, provided that the plan amendment eliminating the optional form of benefit is adopted by the last day of the first plan year beginning on or after December 12, 1994, and is made effective not later than the first day of that plan year, or, if later, 90 days after December 12, 1994. In addition, pursuant to the authority contained in s 7805(b) and s 301.7805-1, the Commissioner has determined that a profit-sharing plan or stock bonus plan will not fail to be qualified merely because the plan (i) contained a provision on or before December 12, 1994, that otherwise satisfied the requirements of s 401(a), and permits the distribution of any portion of an employee's nonforfeitable accrued benefit prior to the employee's retirement, death, disability, or severance of employment, or plan termination, and (ii) applies those provisions to benefits attributable to the assets and liabilities transferred within the meaning of s 414(l) from a qualified money purchase pension plan, provided that the profit-sharing or stock bonus plan is amended by the end of the first plan year beginning on or after December 12, 1994, to preclude distribution options that are not permissible under qualified pension plans from applying to benefits attributable to the assets and liabilities transferred from the money purchase pension plan, and the amendment is made effective not later than the first day of that plan year, or, if later, 90 days after December 12, 1994.

A plan entitled to extended reliance under Rev. Proc. 89-9, 1989-1 C.B. 780, Rev. Proc. 89-13, 1989-1 C.B. 801 (both as modified by Rev. Proc. 93-9, 1993-1 C.B. 474), or Rev. Proc. 93-39, 1993-2 C.B. 513 (relating to master or prototype plans, regional prototype plans, and individually designed plans), will not fail to be entitled to the relief set forth in the preceding paragraph merely because the plan is amended after the date set forth in the preceding paragraph, provided that the following three requirements are satisfied: (i) the plan is amended no later than the last day of the first plan year following the year in which the extended reliance period applicable to the plan ends, (ii) the amendments are made effective no later than the first day of that plan year and no earlier than the first day of the plan year in which the amendments are adopted, and (iii) no transfer of assets and liabilities to the plan from a money purchase pension plan occurred or occurs after the date of the most recent determination letter and prior to the date that the amendments are adopted.

This relief from s 401(a) shall not apply to, or extend any relief otherwise applicable to, any otherwise eligible profit-sharing or stock bonus plan with respect to which the Service has notified the employer(s) (or any authorized agent(s)) prior to December 12, 1994, that the plan did not satisfy the requirements for a qualified plan because it provided for an impermissible distribution of accrued benefits attributable to assets and liabilities transferred from a money purchase pension plan prior to an employee's retirement, death, disability, or severance of employment, or plan termination.

DRAFTING INFORMATION

The principal author of this revenue ruling is Joyce Kahn of the Employee Plans Division. For further information regarding this revenue ruling, please contact the Employee Plans Division's taxpayer

assistance telephone service or Ms. Kahn between the hours of 1:30 and 4 p.m. Eastern time, Monday through Thursday on (202) 622-6074/6075 or (202) 622-6214. (These telephone numbers are not toll-free.)

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