DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

200227041

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

S.I.N.: 4980.00-00, 4980.01.00

APR 9 2002

T:EP:RA:T2

Legend:

Company A
Company B
Company C
State D
State E
Plan X
Plan Y
Adopting
Employers

Dear :

This letter modifies three of the four rulings issued to Company C in PLR 9839030 on June 29, 1998, and in response to the request from your authorized representative dated February 14, 2002, will limit the retroactive effect of such revocation pursuant to section 7805(b) of the Internal Revenue Code.

In a letter dated June 29, 1998, the Internal Revenue Service issued the following private letter rulings to Company C:

1. Plan Y constitutes a replacement plan within the meaning of section 4980(d)(2) of the Code, provided that an amount no less than 25 percent of the excess assets is directly transferred to Plan Y from Plan X.

2. The excess assets transferred from Plan X to Plan Y will not be included in the gross income of Company A or Company C.

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3. No deduction will be allowable with respect to such transfer of excess assets.

4. Such transfer of excess assets will not be treated as an employer reversion under section 4980 of the Code and that there will be no excise tax imposed under section 4980 with respect to the transfer of only 25 percent of the excess assets from Plan X to Plan Y.

Upon reconsideration, we have modified and clarified the second, third, and the first part of the fourth rulings issued on June 29, 1998.

Your authorized representative submitted the following facts and representations on your behalf in a letter dated January 22, 1998, as supplemented by letters dated March 10, 1998, and June 24, 1998, in support of the aforementioned rulings:

Company A is a corporation based in State D. Company C is a wholly-owned subsidiary of Company B, which is a wholly owned subsidiary of Company A. Company C is based in State E. Companies A, B, and C are all members of the same controlled group of corporations pursuant to section 414(b) of the Code.

Companies A and C sponsor Plan X, a defined benefit plan that employers of the controlled group may adopt. Several employers of the controlled group, the Adopting Employers, have adopted Plan X. Companies A and C intend to terminate Plan X and to transfer all of the excess assets in Plan X that remain after the payment of all benefits to Plan Y, a defined contribution plan with a cash or deferred arrangement. One hundred percent of the active participants in Plan X who remain employees of the Adopting Employers will be active participants in Plan Y as of the date the excess assets are transferred.

Prior to the transfer of the excess assets from Plan X, Plan Y and its related trust will be amended to provide for a "suspense account" to hold the excess assets. All amounts held in the suspense account, including income thereon, will be used to fund the matching and employer-based contributions for all employees of the Adopting Employers, no less rapidly than ratably over the seven-plan-year period beginning in the year of the transfer. The minimum amount that must be allocated each plan year will be determined by multiplying the amount in the suspense account as of the first day of the plan year by a fraction, the numerator of which is one and the denominator of which is the number of years remaining in the seven-plan-year period. However, if it is not possible to distribute the amounts to the employees of the Adopting Employers within the seven-plan-year period, amounts held in the suspense account will be used to provide matching and base contributions for all participants in Plan Y to the extent necessary.

In reference to the request for rulings, section 4980(a) of the Code provides for a 20 percent excise tax on the amount of any reversion from a qualified plan. Section

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4980(d), as added by the Omnibus Budget Reconciliation Act of 1990, P.L. 101-508, provides, in general, that the excise tax under section 4980(a) shall be increased to 50 percent with respect to any employer reversion from a qualified plan unless the employer establishes or maintains a qualified replacement plan, or the plan provides for benefit increases which take effect immediately on the termination date. Section 4980(d) generally applies to reversions occurring after September 30, 1990.

Section 4980(c)(2) of the Code defines "employer reversion" as the amount of cash and the fair market value of other property received (directly or indirectly) by an employer from the qualified plan.

Section 4980(d)(2) of the Code generally provides the requirements for a plan to be considered a "qualified replacement plan." The plan must be established or maintained by the employer in connection with a qualified plan termination and at least 95 percent of the active participants in the terminated plan who remain as employees of the employer after the termination are active participants in the replacement plan. Additionally, a direct transfer must be made from the terminated plan to the replacement plan before any "employer reversion," and the transfer must be in an amount equal to 25 percent of the maximum amount the employer could receive as an "employer reversion."

Section 4980(d)(2)(C)(1) of the Code provides that, if the replacement plan is a defined contribution plan, the amount transferred to the replacement plan must be: (I) allocated under the plan to the accounts of participants in the plan year in which the transfer occurs; or (II) credited to a suspense account and allocated from such account to accounts of participants no less rapidly than ratably over the seven plan year period beginning with the year of the transfer. Section 4980(d)(4)(B) provides, in part, that the allocation of any amount (or income allocable thereto) to any account under section 4980(d)(2)(C) shall be treated as an annual addition for purposes of section 415.

The Service concluded in the June 29,1998, letter that the entire Plan X excess assets may be transferred to Plan Y. Furthermore, the June 29, 1998, letter concluded that as long as at least 25 percent of the excess assets is transferred to Plan Y, there would be no excise tax imposed on that 25 percent. However, an excise tax at the rate of 20 percent would be imposed on the remaining 75 percent of the excess assets even if part or all of the remaining 75 percent is transferred to Plan Y.

However, after a subsequent review of the language stated in the previous paragraph, the Service concludes, as a clarification, that only an amount equal exactly to 25 percent of excess would meet the assets transfer requirement stated in section 4980(d)(2)(B) of the Code and could be transferred to Plan Y under the terms of section 4980. In other words, only an amount equal to exactly 25 percent of the excess amounts would not be subject to the excise tax under section 4980. The remaining 75 percent of the excess amounts would be subject to an excise tax equal to 20 percent as provided in section 4980(d). Any excess amounts over the 25 percent would not meet

the assets transfer requirements of section 4980, but could possibly be transferred as a contribution, for example, provided the transfer meets the requirements of section 404 and section 415.

With specific reference to your first ruling request, your authorized representative asserts that all of the employees of the Adopting Employers who are active participants in Plan X and who will remain employees of the Adopting Employers after the termination of Plan X will be active participants in Plan Y. Furthermore, 25 percent of the excess assets remaining after the termination of Plan X will be directly transferred to the trust which holds the Plan Y assets. These representations indicate that, with respect to Plan Y, the requirements of section 4980(d)(2) will be met.

Accordingly, with respect to the first ruling request, we conclude, as in the letter issued June 29,1998, that Plan Y constitutes a qualified replacement plan within the meaning of section 4980(d)(2), provided an amount equal to 25 percent of the excess assets are transferred to Plan Y.

With respect to the second, third and the first part of the fourth ruling requests, section 4980(d)(2)(B)(iii) of the Code provides that in the case of any amount transferred under section 4980(d)(2)(B), (I) such amount shall not be includible in the gross income of the employer, (II) no deduction shall be allowable with respect to such transfer, and (III) such transfer shall not be treated as an employer reversion for purposes of section 4980.

As noted previously, the Service has concluded, as a clarification, that only an amount equal to exactly 25 percent of the excess amount would meet the asset transfer requirements stated in section 4980(d)(2)(B) of the Code ("the 25 Percent Transferred Amount"). Thus, the requirements provided in sections 4980(d)(2)(B)(iii)(I), (II) and (III) would apply only to the 25 Percent Transferred Amount.

Accordingly, we conclude with respect to the second ruling request that only the 25 percent Transferred Amount transferred from Plan X to Plan Y will not be included in the gross income of Company A and Company C. However, assets in excess of the 25 Percent Transferred Amount would be included in the gross income of Company A and Company C.

With respect to the third ruling request, we conclude that no deduction will be allowable with respect to the 25 Percent Transferred Amount. However, any surplus amounts transferred from Plan X to Plan Y in excess of 25 Percent Transferred Amount are considered as contributions to Plan Y that are subject to the deduction rules of section 404 of the Code.

With respect to the first part of the fourth ruling request, we conclude that only the Transferred Amount will not be treated as an employer reversion under section 4980 of the Code.

Concerning the second part of the fourth ruling request, section 4980(d)(2)(B)(i)(I) of the Code provides that an amount equal to 25 percent of the excess assets which an employer could receive from the terminated defined benefit plan must be transferred to the replacement plan. As noted previously, as long as at least 25 percent of the excess assets is transferred to Plan Y, there will be no excise tax imposed on that 25 percent. However, an excise tax at the rate of 20 percent will be imposed on the remaining 75 percent that is transferred to Plan Y.

Accordingly, with respect to the second part of the fourth ruling request, we conclude, as previously, that there will be no excise tax imposed under section 4980 of the Code with respect to the transfer of only 25 percent of the excess assets from Plan X to Plan Y. However, an excise tax at the rate of 20 percent will be imposed on the remaining 75 percent of the excess assets even if part or all of the remaining 75 percent is transferred to Plan Y.

Section 7805(b) of the Code provides that the Secretary may prescribe the extent, if any, to which any ruling or regulations relating to the internal revenue laws, shall be applied without retroactive effect.

Section 13.04 of Revenue Procedure 2002-4, 2002-1 I.R.B. 127, provides that a letter ruling found to be in error or not in accord with the current views of the Service may be revoked or modified. If a letter ruling is revoked or modified, the revocation or modification applies to all years open under the statute of limitations, unless the Service uses its discretionary authority under section 7895(b) of the Code to limit the retroactive effect of the revocation or modification.

Section 13.05 of Revenue Procedure 2002-4 provides that, except in rare or unusual circumstances, the revocation or modification of a letter ruling will not be applied retroactively to the taxpayer for whom the ruling was issued or to a taxpayer whose tax liability was directly involved in the ruling provided that (1) there has been no misstatement or omission of material facts, (2) the facts at the time of the transaction are not materially different from the facts on which the letter ruling was based, (3) there has been no change in the applicable law, (4) the letter ruling was originally issued for a prospective transaction, and (5) the taxpayer directly involved the letter ruling acted in good faith in relying on the letter ruling, and revoking or modifying the ruling retroactively would be to the taxpayer's detriment.

Based on the review of the applicable law and the information provided to us in your authorized representative's April 5, 2000 letter, we have concluded that the five conditions of section 13.05 of Revenue Procedure 2002-4 have been met. Therefore, pursuant to the authority contained in section 7805(b) of the Code, the holding of this letter will not be applied retroactively to transactions that occurred prior to March 31, 2000, the date that the taxpayer received written notice that the Service was reconsidering Private Letter Ruling Number 9839031 dated June 29, 1998.

This letter is directed only to the transactions that transpired prior to March 31, 2000, and were completed in reliance of the June 29,1998, letter.

This ruling is directed only to the taxpayer who requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited by others as precedent.

Should you have any questions please contact

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A copy of this letter is being sent to your authorized representative in accordance the power of attorney on file in this office.

Sincerely,

/s/ Paul T. Shultz

Paul T. Shultz, Director
Employees Plan, Rulings and Agreements

Enclosures:
Form 437
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