200038057

Internal Revenue Service

Department of the Treasury

SIN = 402.07-00

Washington, DC 20224

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Person to Contact: xxxxx

Telephone Number: xxxxx

Refer Reply to: T:EP:RA:T2/50-06967

Date: JUN 28 2000

Legend:
Taxpayer A = xxxxx

Employer M = xxxxx

State B = xxxxx

Plan X = xxxxx

Dear xxxxx:

This is in response to a letter dated xxxxx, 1999, as supplemented and amended by letters dated xxxxx, 1999, xxxxx, 1999, xxxxx, 1999, xxxxx, 1999, xxxxx, 2000, and xxxxx, 2000, and telephone conferences on xxxxx, 2000, and xxxxx, 2000, in which your authorized representative requested rulings on your behalf in your capacity as an individual taxpayer and as Chairman & CEO of Employer M regarding the Federal income tax treatment of certain distributions from a defined contribution plan that includes an employee stock ownership plan (ESOP).

Employer M, a banking institution under the laws of State B, maintains Plan X for the benefit of its employees, including Taxpayer A. Plan X was established as a profit-sharing plan on October 24, 1947, and is qualified pursuant to section 401(a) of the Internal Revenue Code. Employer M later added a cash or deferred arrangement (CODA) described in section 401(k)(2) of the Code to Plan X. When Employer M became a subsidiary of a public company in xxxx, it allowed individual Plan X participants to direct that limited amounts of stock be acquired for their respective accounts at that time. Other employees subsequently desired to acquire stock, and ultimately Plan X was amended in 1995 to create an ESOP within the meaning of section 4975(e)(7) of the Code to operate in conjunction with the profit-sharing plan. Employer M maintained a money

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4975(e)(7) of the Code to operate in conjunction with the profit-sharing plan. Employer M maintained a money purchase pension plan at one time but it was terminated when the CODA was added to Plan X.

Distributions from Plan X are to be made pursuant to section 401(a)(9) of the Code. A Plan X participant may elect to receive a distribution from his or her ESOP account in the form of qualified employer securities. Plan X allows for the direct rollover of amounts from Plan X to an eligible retirement plan or for distribution of a portion of a participant's account balance in cash with the remainder of such account balance rolled over to an eligible retirement plan.

Taxpayer A is the Chairman and Chief Executive Officer of Employer M. He was born in 1934, has participated in Plan X for at least five tax years, and attained normal retirement age under the terms of Plan X in 1999. Under Plan X, the normal retirement age is 65. Although eligible to retire, Taxpayer A does not intend to retire at this time. However, in accordance with the terms of Plan X, Taxpayer A does intend to withdraw his funds from Plan X on account of attaining normal retirement age.

All Employer M stock is held in the ESOP. Any assets or investments other than employer stock that are held in the ESOP consist of deposits and/or marketable securities, and are used to buy Employer M stock. Any assets or investments other than employer stock that are held in the ESOP are identical to the assets or investments of the profit-sharing portion of Plan X. Plan X allows for a transfer twice a year between the profit-sharing portion and ESOP portion of Plan X of any assets or investments, other than employer stock.

Taxpayer A wants to exclude the net unrealized appreciation (NUA) on employer stock distributed from the ESOP from his gross income pursuant to section 402(e)(4) of the Code. In an effort to avoid other tax liability, Taxpayer A intends for Plan X to make a direct transfer of his shares of employer stock with the highest cost basis to an IRA. The remaining shares will be distributed to Taxpayer A. In addition, Taxpayer A intends to have some or all ESOP assets or investments, other than employer stock, transferred to the profit-sharing portion of Plan X during the twice a year transfer period provided for in

Plan X, as explained above. The other investments not transferred to the profit-sharing portion will be transferred to an IRA.

In the same tax year that Taxpayer A empties his ESOP account to reflect a zero balance, Taxpayer A also will empty the assets held in the profit-sharing plan portion of Plan X by having all or a portion of his profit-sharing balance transferred through a direct rollover to an IRA and have the remainder of assets in the profit-sharing plan distributed to him.

Based on the facts and representations provided herein, the following rulings have been requested:

1. That the tax-free transfer of some, if not all, of the assets held in the profit-sharing plan portion of Plan X to an IRA and the distribution to Taxpayer A of any amount in the profit-sharing plan portion that is not transferred by a trustee-to-trustee rollover, after Taxpayer A has reached age 59 1/2 and within the same tax year that Taxpayer A receives a distribution of all of his employer stock account by having all or a portion of his employer stock credited in his name distributed to him and the transfer of the remaining employer stock and any other investment held in the ESOP (other than those other investments that are transferred to the profit-sharing portion of Plan X) to an IRA pursuant to a trustee-to-trustee rollover, will not adversely affect the classification of the ESOP distribution as a lump sum distribution pursuant to Code sections 402(d)(4)and 402(e)(4).

2. That the distribution of some of the employer stock credited in Taxpayer A's name in the ESOP portion of Plan X and the transfer of the remaining employer stock or any other investments held in the ESOP (other than those other investments that are transferred as described above to the profit-sharing portion of Plan X) to an IRA pursuant to a trustee-to-trustee rollover, will not adversely affect the classification of the ESOP distribution as a lump sum distribution pursuant to Code sections 402(d)(4) and 402(e)(4).

3. That Taxpayer A may exclude from gross income all NUA related to employer stock distributed to him pursuant to Code sections 402(d)(4) and 402(e)(4) from the ESOP portion of Plan X until such stock is disposed of by Taxpayer A,

notwithstanding the tax-free transfer of some or all of the assets held in his name in the profit-sharing plan portion of Plan X, or the transfer of some employer stock or other investments held in the ESOP directly into an IRA. If less than all of the profit-sharing plan portion is transferred to an IRA, the rest will be distributed to Taxpayer A during the same taxable year.

Code section 402(a) provides a general rule which states that, except as otherwise provided in section 402, any amount actually distributed to any distributee by any employees' trust described in Code section 401(a) which is exempt from tax under Code section 501(a) shall be taxable to the distributee, in the taxable year of the distributee in which distributed, under Code section 72 (relating to annuities).

Code section 402(e)(4)(B) provides that in the case of any lump sum distribution that includes securities of the employer corporation, the NUA on those securities is excluded from the distributee's gross income unless otherwise elected by the distributee.

Code section 402(e)(4)(D)(i), effective for tax years beginning after 12/31/99, provides the definition of "lump sum distribution". The pertinent language of the definition of "lump sum distribution" is identical to section 402(d)(4)(A) which applied to tax years before 1/1/2000.

Code section 402(e)(4)(D)(i) defines a "lump sum distribution" as the distribution or payment within 1 taxable year of the recipient of the balance to the credit of an employee which becomes payable to the recipient--

(i) on account of the employee's death,
(ii) after the employee attains age 59 1/2,
(iii) on account of the employee's separation from service, or
(iv) after the employee has become disabled (within the meaning of Code section 72(m)(7),

from a trust which forms a part of a plan described in section 401(a) and which is exempt from tax under section 501 or from a plan described in section 403(a).

Code section 402(c)(1) provides that if --

(A) any portion of the balance to the credit of an employee in a qualified trust is paid to the employee in an eligible rollover distribution,

(B) the distributee transfers any portion of the property received in such distribution to an eligible retirement plan, and

(C) in the case of a distribution of property other than money, the amount so transferred consists of the property distributed,
then such distribution (to the extent so transferred) shall not be includible in gross income for the taxable year in which paid.

Pursuant to Code section 402(c)(4), a lump sum distribution under section 402(e)(4)(D)(I) constitutes an eligible rollover distribution.

Code section 401(a)(31)(A) provides, in general, that a trust shall not constitute a qualified trust under this section unless the plan of which such trust is a part provides that if the distributee of any eligible rollover distribution --

(i) elects to have such distribution paid directly to an eligible retirement plan, and
(ii) specifies the eligible retirement plan to which such distribution is to be paid (in such form and at such time as the plan administrator may prescribe),

such distribution shall be made in the form of a direct trustee-to trustee transfer to the eligible retirement plan so specified.

The definition of an eligible rollover distribution found under Code section 402(c)(4) is used for purposes of Code section 401(a)(31).

The disposition within one taxable year of a participant's account balance in Plan X through a combination of trustee-to-trustee transfers from the profit-sharing portion or ESOP portion to an IRA and distributions from the profit-sharing portion or ESOP

portion to the participant does not preclude such disposition from qualifying as a lump sum distribution.

Neither the Code nor the regulations promulgated under Code sections 402(d)(4)(A) and 402(e)(4)(D)(i) precludes a distribution from being treated as a lump sum under those sections for purposes of Code section 402(e)(4)(B) even if a portion of the distribution is either transferred directly or rolled over into an IRA or into another qualified plan pursuant to Code section 401(a)(31) or Code section 402(c).

Taxpayer has attained age 59 ½, has been a participant in Plan X for at least 5 years and intends to receive the balance to his credit in both the profit-sharing portion and ESOP portion of Plan X within one taxable year.

Accordingly, with respect to ruling request one, we conclude that the tax-free transfer of some, if not all, of the assets held in the profit-sharing plan portion of Plan X to an IRA and the distribution to Taxpayer A of any amount in the profit-sharing plan portion that is not transferred by a trustee-to-trustee rollover, after Taxpayer A has reached age 59 1/2 and within the same tax year that Taxpayer A receives a distribution of all of his employer stock account by having all or a portion of his employer stock credited in his name distributed to him and the transfer of the remaining employer stock and any other investment held in the ESOP (other than those other investments that are transferred to the profit-sharing portion of Plan X) to an IRA pursuant to a trustee-to-trustee rollover, will not adversely affect the classification of the ESOP distribution as a lump sum distribution pursuant to Code sections 402(d)(4)and 402(e)(4).

With respect to ruling request two, we conclude that the distribution of some of the employer stock credited in Taxpayer A's name in the ESOP portion of Plan X and the transfer of the remaining employer stock or any other investments held in the ESOP (other than those other investments that are transferred as described above to the profit-sharing portion of Plan X) to an IRA pursuant to a trustee-to-trustee rollover, will not adversely affect the classification of the ESOP distribution as a lump sum distribution pursuant to Code sections 402(d)(4) and 402(e)(4).

With respect to ruling request three, we conclude that Taxpayer A may exclude from gross income all NUA related to employer stock distributed to him pursuant to Code sections 402(d)(4) and 402(e)(4) from the ESOP portion of Plan X until such stock is disposed of by Taxpayer A, notwithstanding the tax-free transfer of some or all of the assets held in his name in the profit-sharing plan portion of Plan X, or the transfer of some employer stock or other investment held in the ESOP directly into an IRA. If less than all of the profit-sharing plan portion is transferred to an IRA, the rest will be distributed to Taxpayer A during the same taxable year.

This ruling is based on the assumption that Plan X will be qualified under Code section 401(a) and its trust will be exempt under Code section 501(a) at all times pertinent to the transaction.

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

Sincerely yours,

(signed) JOYCE E. FLOYD

Joyce E. Floyd, Manager
Employee Plans Technical Group 2
Tax Exempt and Government Entities
Division

Enclosures:
Deleted copy of ruling letter
Notice of Intention to Disclose

cc: