Internal Revenue Service

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Department of the Treasury

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Washington, DC 20224

Person to Contact:

Telephone Number:

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In re:

This is in response to your request for a ruling regarding a proposed transaction between a pension plan sponsored by the above-named corporation (the "taxpayer's plan") and a multi-employer plan (of which the above-named corporation is a contributing sponsor).

FACTS

The taxpayer sponsors a defined benefit pension plan for its employees (other than leased employees and such employees who are covered under a collective bargaining agreement). The taxpayer also contributes to a defined benefit multi-employer plan which provides benefits to those of the taxpayer's employees who are covered under a collective bargaining agreement. Both plans are qualified plans under section 401 of the Internal Revenue Code ("Code"). Also, both plans are subject to Title IV of the Employee Retirement Income Security Act of 1974 ("ERISA") applies.

Actuarial projections indicate that the multi-employer plan will become insolvent within several years. The trustees of the multi-employer plan, along with the associated union, the contributing employers (including the taxpayer) and the Pension Benefit Guaranty Corporation entered into an agreement (the "Agreement") that is intended to keep the multi-employer plan solvent for several additional years. One provision of the Agreement calls for the multi-employer plan to identify employee groups whose liabilities might be transferred to overfunded defined benefit plans, and to use its best efforts to effect such transfers.

The taxpayer proposes to have liabilities under the multi-employer plan attributable to its employees transferred into the taxpayer's plan, which is an overfunded single-employer plan ("overfunded plan"). The taxpayer's plan is overfunded (on a termination basis) by an amount which exceeds the present value of the liabilities that would be transferred from the multi-employer plan. The group of employees that was covered by the overfunded plan is different from the group that was covered by the multi-employer plan.

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As a result of the proposed transfer, the taxpayer will be relieved of any withdrawal liability that might otherwise have been imposed under subtitle E of title IV of ERISA. In the instant case, the amount of the withdrawal liability is approximately 90% of the value of the transferred liabilities and, as a result of the proposed transfer, the withdrawal liability that would otherwise be imposed on the taxpayer will be reduced to zero.

REQUESTED RULINGS

1) Will the transfer of benefit liabilities from the multi-employer plan into the taxpayer's plan, and the subsequent payment of such benefits from the taxpayer's plan, cause the taxpayer to recognize income for purposes of the federal income tax?

2) Will the transfer of liabilities constitute a reversion (whether deemed or actual) of pension assets that would cause the taxpayer to be liable for the excise tax imposed under section 4980 of the Code?

LAW

Section 61 of the Code provides that "gross income" is defined to include all income from whatever source derived (except as otherwise provided in Subtitle A of the Code).

Section 111(a) of the Code provides that gross income does not include income attributable to the recovery during the taxable year of any amount deducted in any prior taxable year to the extent such amount did not reduce the amount of tax imposed by this chapter. This section constitutes the codification of the so-called exclusionary portion of the tax benefit rule.

The balance of the tax benefit rule, known as the "inclusionary" portion, has been clarified in Rev. Rul. 68-104 (1968-1 C.B., 361), which provides that "where amounts previously deducted from gross income (which thereby effected a tax benefit) are recovered in subsequent years, such recoveries are includible gross income for the year of recovery". This so-called "tax benefit rule" was originally fashioned by the judiciary in order to approximate the results produced by a tax system based on transactional, rather than annual, accounting. The rule was applied by the United States Supreme Court in Hillsboro National Bank v. Commissioner, 460 U.S. 370 (1983). The tax benefit rule, as formulated in this decision, provides that a taxpayer includes income when an event occurs which is "fundamentally inconsistent" with a deduction taken in a prior year, unless a nonrecognition provision of the Code prevents inclusion. Thus, under Hillsboro, an

actual recovery of the amount in question is not necessary. The determination that must be made under the Hillsboro test is whether the subsequent event would have foreclosed the earlier deduction if the subsequent event and the event giving rise to the deduction had occurred in the same year. If the subsequent event would have foreclosed the deduction, the event is fundamentally inconsistent and the taxpayer must include the amount as income in the year of the subsequent event.

Sections 401(a)(12) and 414(l)(1) of the Code provide, in part, that a trust which forms part of a plan shall not constitute a qualified trust under section 401 unless in the case of any merger or consolidation of the plan with, or in the case of any transfer of assets or liabilities of such plan to, any other trust plan, each participant in the plan would (if the plan then terminated) receive a benefit immediately after the merger, consolidation or transfer which is equal to or greater than the benefit he would have been entitled to receive immediately before the merger, consolidation, or transfer (if the plan had then terminated). However, this requirement does not apply to any multi-employer plan with respect to any transaction to the extent that participants either before or after the transaction are covered under a multi-employer plan to which Title IV of ERISA applies.

Code section 4980 imposes an excise tax in the event of an employer reversion from a qualified plan. Under Code section 4980(c)(2)(A), the term "employer reversion" is defined generally to mean the amount of cash and the fair market value of other property received (directly or indirectly) by an employer from the qualified plan.

ANALYSIS

The use of surplus funds in the overfunded plan to fund benefits attributable to the taxpayer's collectively-bargained employees (which would otherwise be funded in part by future payments of withdrawal liability under subtitle E of title IV of ERISA) is consistent with the use that was intended when deductions were claimed under Code section 404 for contributions to the taxpayer's plan. Accordingly, we conclude that the proposed transfer of liabilities will not cause the taxpayer to recognize income for purposes of the federal income tax. Under the same analysis, we find that this transfer of liabilities will not create an employer reversion within the meaning of Code section 4980.

CONCLUSION

Subject to the caveat that this proposed transfer of liabilities will not cause a violation of Code section 401(a)(12) and 414(l) with respect to the non-collectively-bargained participants under the taxpayer's plan, we find that (i) the proposed transfer will

not cause the taxpayer to recognize income for purposes of the federal income tax and (ii) the proposed transfer will not create an employer reversion within the meaning of Code section 4980.

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

Sincerely,

Carol Gold
Director, Employee Plans Division