# Section 401.—Qualified Pension, Profit-Sharing, and Stock Bonus Plans

*(Also, §§ 411, 4980F; 26 CFR 1.411(d)–2.)*

# Rev. Rul. 2002–42

**Merger or conversion; partial termination; notice**. This ruling describes a situation where a merger or conversion of a money purchase pension plan into a profit-sharing plan is not a partial termination of the money purchase pension plan and also describes the type of notice that must be given to affected plan participants.

ISSUES

1. Whether, in the absence of other facts indicating a partial termination, the merger or conversion of a money purchase pension plan into a profit-sharing plan results in a partial termination of the money purchase pension plan under § 411(d)(3) of the Internal Revenue Code (the Code).

2. Whether the notice required by § 4980F of the Code and section 204(h) of the Employee Retirement Income Security Act of 1974, as amended (ERISA) must be provided to affected individuals in a money purchase pension plan that is merged or converted into a profit-sharing plan.

FACTS

Situation 1. Employer J maintains a money purchase pension plan qualifying under § 401(a) of the Code. The plan provides that upon a termination or partial termination of the plan, all affected participants will vest 100% in their account balances. Employer J converts the money purchase pension plan into a profit-sharing plan that covers the same employees as the money purchase pension plan and contains the same vesting schedule. It also provides that assets and liabilities in the profit-sharing plan that originated in the money purchase pension plan retain their money purchase pension plan attributes, in accordance with Rev. Rul. 94–76, 1994–2 C.B. 46.

Situation 2. Employer L maintains a money purchase pension plan qualifying under § 401(a). This plan provides that upon a termination or partial termination of the plan all affected participants will vest 100% in their account balances. Employer L also maintains a profit-sharing plan qualifying under § 401(a). L amends the money purchase pension plan to cease future employer contributions and to merge it into the profit-sharing plan in a transaction that satisfies the requirements of § 414(*l*). Following the merger, the profit-sharing plan covers the same employees and contains the same vesting schedule as the money purchase pension plan. Simultaneously, L amends the profit-sharing plan to provide that assets and liabilities transferred from the money purchase pension plan to the profit-sharing plan retain their money purchase pension plan attributes, in accordance with Rev. Rul. 94–76.

LAW AND ANALYSIS

*Section 411(d)(3)*

Section 411(d)(3) requires that a plan provide that upon its termination or partial termination the rights of all affected parties accrued to the date of such termination or partial termination, to the extent funded as of such date, or the amounts credited to the employees' accounts, are nonforfeitable.

Section 1.411(d)–2(b)(1) of the Income Tax Regulations provides that whether or not a partial termination of a defined contribution or defined benefit plan has occurred is dependent on the facts and circumstances in a particular case. Such facts and circumstances include: the exclusion, by reason of a plan amendment or severance by the employer, of a group of employees who have previously been covered by the plan; and plan amendments which adversely affect the rights of employees to vest in benefits under the plan. Section 1.411(d)–2(b)(2) contains a special rule providing that if a defined benefit plan ceases or decreases future benefit accruals under the plan, a partial termination shall be deemed to occur if, as a result of such cessation or decrease, a potential reversion to the employer maintaining the plan (determined as of the date such cessation or decrease is adopted) is created or increased.

Section 1.401(a)–2(b) provides that a plan may provide that upon the plan's termination assets held in a § 415 suspense account may revert to the employer.

Section 1.415–6(b)(6) describes how amounts in a § 415 suspense account must be allocated to participants before any amount in the § 415 suspense account may revert to the employer on plan termination.

Rev. Rul. 85–6, 1985–1 C.B. 133, provides that a defined benefit plan that has surplus resulting from actuarial error may allow that surplus to revert to the employer upon termination of the plan.

Rev. Rul. 80–155, 1980–1 C.B. 84, provides that a profit-sharing, stock bonus, or money purchase pension plan (*i.e.*, a defined contribution plan) will not satisfy plan qualification requirements unless all funds are allocated to participants' accounts under the plan in accordance with a definite formula (although certain exceptions are allowed, such as the use of a suspense account in accordance with the requirements of § 415 of the Code).

Rev. Rul. 94–76 provides that, under § 414(*l*), the transfer of assets and liabilities from a money purchase pension plan to a profit-sharing plan is considered a spinoff of those assets and liabilities from the money purchase pension plan and a merger of those assets and liabilities with the assets and liabilities of the profit-sharing plan. The merger does not divest the assets and liabilities of the money purchase pension plan of their attributes as money purchase pension plan assets and liabilities. The holding in Rev. Rul. 94–76 is applicable when an employer converts a money purchase pension plan into a profit-sharing plan.

The special rule provided in § 1.411(d)–2(b)(2) for determining whether a partial termination has occurred is limited to defined benefit plans. The listed facts and circumstances in § 1.411(d)–2(b)(1) do not include the creation of a potential reversion as a factor to be considered in determining whether there has been a partial termination of a defined contribution plan. Unlike a defined benefit plan, in a defined contribution plan all assets must be allocated to participants' accounts with the exception of amounts held in a § 415 suspense account. Therefore, on the termination of a defined contribution plan, the only amounts that may revert to the employer are amounts in a § 415 suspense account and then only to the extent amounts in the § 415 suspense account are not required to be allocated as provided under § 1.415–6(b)(6). In a defined contribution plan, the cessation or reduction of benefit accruals does not create or increase the potential for reversion. Accordingly, the creation or increase of a potential reversion is not a relevant fact or circumstance in determining whether there has been a partial termination in a defined contribution plan as a result of the cessation or reduction of benefit accruals.

In Situations 1 and 2, all of the employees who are covered by the converted or merged money purchase plan remain covered under the continuing profit-sharing plan, the money purchase plan assets and liabilities retain their characterization under the profit-sharing plan, and the employees vest in the continuing profit-sharing plan under the same vesting schedule that existed under the money purchase plan. Under these facts and circumstances, no partial termination has occurred.

*Section 4980F of the Code and § 204(h) of ERISA*

ERISA § 204(h), as amended by § 659(b) of the Economic Growth and Tax Relief Reconciliation Act of 2001, Public Law 107–16 (EGTRRA), provides that a defined benefit pension plan or an individual account plan subject to the funding standards of § 412 of the Code not be amended to provide a significant reduction in the rate of future benefit accrual unless the plan administrator provides a notice describing the reduction to each affected individual whose benefit is adversely affected by the reduction and to each employee organization representing these individuals.

Section 4980F, as added by § 659(a) of EGTRRA, provides for an excise tax if a defined benefit pension plan or an individual account plan subject to the funding standards of § 412 is amended to provide a significant reduction in the rate of future benefit accrual and the plan administrator does not provide a notice describing the reduction to each affected individual whose benefit is adversely affected by the reduction and to each employee organization representing these individuals.

If a money purchase plan is converted or merged into a profit-sharing plan, there is necessarily a significant reduction in the rate of future benefit accrual under the money purchase plan requiring notice under § 4980F of the Code and § 204(h) of ERISA. Allocations under the profit-sharing plan are not benefit accruals under the money purchase plan for purposes of determining if there is a reduction in the rate of future benefit accrual for purposes of § 4980F of the Code and § 204(h) of ERISA. A profit-sharing plan is neither subject to § 4980F of the Code or § 204(h) of ERISA. Consequently, a notice is required to be given to affected individuals under § 4980F of the Code and § 204(h) of ERISA.

## HOLDINGS

Issue 1. In the absence of other facts, the merger or conversion of a money purchase pension plan into a profit-sharing plan does not result in a partial termination of the money purchase pension plan under § 411(d)(3) of the Code. Under either the facts in Situation 1 or 2 there is no partial termination.

Issue 2. The notice required by § 4980F of the Code and § 204(h) of ERISA must be provided to affected individuals in a money purchase pension plan that is merged or converted into a profit-sharing plan. Under the facts in either Situation 1 or 2, the notice must be given to affected individuals.

## EFFECT ON OTHER REVENUE RULINGS

Rev. Rul. 94–76 is amplified.

## DRAFTING INFORMATION

The principal author of this revenue ruling is Andrew Zuckerman of the Employee Plans, Tax Exempt and Government Entities Division. For further information regarding this revenue ruling, please contact the Employee Plans' taxpayer assistance telephone service at 1–877–829–5500 (a toll-free number), between the hours of 8:00 a.m. and 6:30 p.m. Eastern time, Monday through Friday. Mr. Zuckerman may be reached at 1–202–283–9655 (not a toll-free number).