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IRS ISSUES REVENUE RULING ON MERGER OR CONVERSION OF MONEY PURCHASE PLAN INTO PROFIT-SHARING PLAN

[14815] June 20, 2002 TO: PENSION MEMBERS No. 29-02 PENSION OPERATIONS ADVISORY COMMITTEE No. 39-02 RE: IRS ISSUES REVENUE RULING ON MERGER OR CONVERSION OF MONEY PURCHASE PLAN INTO PROFIT-SHARING PLAN The Internal Revenue Service recently issued Revenue Ruling 2002-42, which provides guidance on two issues relating to the merger or conversion of a money purchase pension plan into a profit-sharing plan: (1) whether a merger or conversion results in a partial termination of the money purchase plan under Code section 411(d)(3), and (2) whether the notice required by Code section 4980F and ERISA section 204(h) must be provided to affected individuals in the case of such merger or conversion. Partial termination issue. The revenue ruling holds that in the absence of other facts, the merger or conversion of a money purchase plan into a profit-sharing plan does not result in a partial termination of the money purchase plan under Code section 411(d)(3). Applying this rule to the facts presented, the revenue ruling provides that a partial termination would not occur upon such a merger or conversion where (1) all of the employees who are covered by the converted or merged money purchase plan remain covered under the continuing profit-sharing plan, (2) the money purchase plan assets and liabilities retain their character under the profit- sharing plan pursuant to Revenue Ruling 94-76,1 and (3) the employees vest in the continuing profit-sharing plan under the same vesting schedule that applied to the money purchase plan. In reaching its conclusion, the IRS observed that in a defined contribution plan, the cessation or reduction of benefit accruals does not create or increase the potential for reversion to an employer — a factor that would determine whether a partial termination of a defined benefit plan has occurred.2 Notice requirement. The revenue ruling provides that where a money purchase plan is converted or merged into a profit-sharing plan, there is necessarily a significant reduction in the 1 Revenue Ruling 94-76 provides that under Code section 414(l), the transfer of assets and liabilities from a money purchase plan to a profit-sharing plan is considered a spinoff of those assets and liabilities from the money purchase plan and the merger of those assets and liabilities into the profit-sharing plan. Accordingly, the IRS ruled that the transferred assets and liabilities are not divested of their attributes and therefore remain subject to the restrictions on distributions applicable to money purchase plans. See 1994-2 C.B. 46, 1994-50 I.R.B. 5. 2 See Treas. Reg. 1.411(d)-2(b)(2). 2 rate of future benefit accrual under the merged or converted money purchase plan. Thus, the revenue ruling holds that the notice required by Code section 4980F and ERISA section 204(h) must be provided to affected individuals. Thomas T. Kim Associate Counsel

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