

Revenue Ruling 2007-43

Part I

Section 411. ----Minimum Vesting Standards

26 CFR 1.411(d)-2: Termination or partial termination; discontinuance of contributions.

Rev. Rul. 2007-43

ISSUE

Is there a partial termination of a plan under § 411(d)(3) of the Internal Revenue Code under the facts described in this revenue ruling?

FACTS

Employer X maintains Plan A, a defined contribution plan qualified under § 401(a). The plan year for Plan A is the calendar year. The plan participants include both current and former employees. Plan A provides that an employee of Employer X has a fully vested and nonforfeitable interest in his or her account balance upon either completion of 3 years of service or attainment of age 65. The plan also provides for each participant to have a fully vested and nonforfeitable right to his or her account balance upon the plan's termination or upon a partial termination of the plan that affects the participant.

Employer X ceases operations at one of its four business locations. As a result, 23 percent of the Plan A participants who are employees of Employer X cease active participation in Plan A due to a severance from employment (excluding any severance from employment that is either on account of death or disability, or retirement on or after normal retirement age) during the plan year. Some of these participants are fully vested due to having completed 3 years of service or having attained age 65. Plan A is not terminated.

LAW

Section 411(d)(3) provides in relevant part that a plan will not be qualified unless the plan provides that, upon its partial termination, the rights of all affected employees to benefits accrued to the date of such partial termination, to the extent funded on that date, or the amounts credited to their 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 qualified plan occurs (and the time of such event) is determined by the Commissioner with regard to all the facts and circumstances in a particular case. The 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, as well as plan amendments that adversely affect the rights of employees to vest in benefits under the plan.

Section 1.411(d)-2(b)(2) provides a special rule with respect to a defined benefit plan that ceases or decreases future benefit accruals under the plan. A partial termination is deemed to occur if a potential reversion to the employer maintaining the plan is created or increased as a result of such cessation or decrease. This special rule does not apply to defined contribution plans.

Section 1.411(d)-2(b)(3) provides that, if a termination occurs, § 411(d)(3) only applies to the part of the plan that is terminated.

In Rev. Rul. 73-284, 1973-2 C.B. 139, an employer established a qualified pension plan that covered all of its 15 employees. The employer later acquired a new business location 100 miles away and closed the original one. All employees were given the opportunity to transfer to the new location and continue to participate in the plan, but only 3 chose to do so. The other 12 employees were discharged and their participation under the plan ended. The employer hired replacements for them at the new location. The revenue ruling concludes that there was a partial termination due to the termination of these employees in connection with the change in business location.

In Rev. Rul. 81-27, 1981-1 C.B. 228, the employer established a qualified defined benefit pension plan that covered employees in the two divisions of its businesses. The plan covered 165 employees. The employer closed down one division and terminated 95 participants. The revenue ruling concludes that the discharge by the employer of 95 of 165 participants constituted a partial termination.

Weil v. Terson Co. Retirement Plan Administrative Committee, 933 F.2d 106 (2d Cir. 1991), holds that the turnover rate in both vested and nonvested participants is taken into account in determining whether there has been a reduction in the workforce that constitutes a partial termination for purposes of § 411(d)(3). See 933 F.2d at 110.

Matz v. Household International Tax Reduction Investment Plan, 388 F.3d 570 (7th Cir. 2004), holds that there is a rebuttable presumption that a 20 percent or greater reduction in plan participants is a partial termination for purposes of § 411(d)(3). The court holds that this presumption is rebuttable depending on other

facts and circumstances. See 388 F.3d at 578. The court, relying on Weil, bases the 20 percent calculation on the ratio of those participants who lose coverage, whether or not vested, to all participants, whether or not vested.

ANALYSIS

Based on the foregoing, whether a partial termination of a plan under § 411(d)(3) has occurred depends on the facts and circumstances, including the extent to which participating employees have had a severance from employment. If the turnover rate is at least 20 percent, there is a presumption that a partial termination of the plan has occurred. The turnover rate is determined by dividing the number of participating employees who had an employer-initiated severance from employment during the applicable period by the sum of all of the participating employees at the start of the applicable period and the employees who became participants during the applicable period. The applicable period depends on the circumstances: the applicable period is a plan year (or, in the case of a plan year that is less than 12 months, the plan year plus the immediately preceding plan year) or a longer period if there are a series of related severances from employment.

All participating employees are taken into account in calculating the turnover rate, including vested as well as nonvested participating employees. Employer-initiated severance from employment generally includes any severance from employment other than a severance that is on account of death, disability, or retirement on or after normal retirement age. An employee's severance from employment is employer-initiated even if caused by an event outside of the employer's control, such as severance due to depressed economic conditions. In certain situations, the employer may be able to verify that an employee's severance was not employer-initiated. A claim that a severance from employment was purely voluntary can be supported through items such as information from personnel files, employee statements, and other corporate records.

Employees who have had a severance from employment with the employer maintaining the plan on account of a transfer to a different controlled group are not considered as having a severance from employment for purposes of calculating the turnover rate if those employees continue to be covered by a plan that is a continuation of the plan under which they were previously covered (i.e., if a portion of the plan covering those employees was spun off from the plan in accordance with the rules of § 414(l) and will continue to be maintained by the new employer).

Whether or not a partial termination of a qualified plan occurs on account of participant turnover (and the time of such event) depends on all the facts and circumstances in a particular case. Facts and circumstances indicating that the turnover rate for an applicable period is routine for the employer favor a finding

that there is no partial termination for that applicable period. For this purpose, information as to the turnover rate in other periods and the extent to which terminated employees were actually replaced, whether the new employees performed the same functions, had the same job classification or title, and received comparable compensation are relevant to determining whether the turnover is routine for the employer. Thus, there are a number of factors that are relevant to determining whether a partial termination has occurred as a result of turnover, both in the case where a partial termination is presumed to have occurred due to the turnover rate being at least 20 percent and in the case where the turnover rate is less than 20 percent.

In the present case, there is a presumption that a partial termination has occurred because the turnover rate is 20 percent or more. The facts and circumstances support the finding of a partial termination because the severances from employment occurred as a result of the shutdown of one of the employer's business locations (and not as a result of routine turnover). Therefore, a partial termination of Plan A has occurred.

If a partial termination occurs on account of turnover during an applicable period, all participating employees who had a severance from employment during the period must be fully vested in their accrued benefits, to the extent funded on that date, or in the amounts credited to their accounts.

A partial termination of a qualified plan can also occur for reasons other than turnover. For example, a partial termination can occur due to plan amendments that adversely affect the rights of employees to vest in benefits under the plan, plan amendments that exclude a group of employees who have previously been covered by the plan, or the reduction or cessation of future benefit accruals resulting in a potential reversion to the employer.

HOLDING

Under the facts described in this revenue ruling, a partial termination has occurred.

DRAFTING INFORMATION

The principal author of this revenue ruling is Ingrid E. Grinde of the Employee Plans, Tax Exempt and Government Entities Division. For further information regarding this revenue ruling, contact the Employee Plans taxpayer assistance answering service between the hours of 8:30 a.m. and 4:30 p.m., Eastern time, Monday through Friday at 1-877-829-5500 (a toll free number) or Ms. Grinde at RetirementPlanQuestions@irs.gov.