Internal Revenue Service

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4973.02-00

Department of the Treasury

Washington, DC 20224

200151051

Person to Contact:

Telephone Number:

Refer Reply to:

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Date:

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LEGEND:

Company A:

Company B:

Taxpayer C:

Company D:

State Agency E:

Court F:

Date 1:

Date 2:

Date 3:

Sum 1:

Ladies and Gentlemen:

This is in response to the request for letter ruling dated , submitted on your behalf by your authorized representative, as supplemented by correspondence dated , and , in which you ask a series of letter ruling requests dealing with the consequences of the transaction summarized below. The following facts and representations support your ruling request.

On Date 1, 2000, Company A was placed into receivership by State Agency E due to a short-fall in assets of approximately Sum 1 which assets had been intended to be held in trust for the benefit of account holders including holders of individual retirement accounts (IRAs) described in section 408 of the Internal Revenue Code. Your authorized representative has provided the Internal Revenue Service with documentation which indicates that the short-fall is alleged to have resulted because of fraud and other tortious actions committed by a related

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financial institution (and/or individuals controlling that institution) that held, in escrow, assets concerning which Company A served as trustee. Company D has been appointed as a receiver of Company A, and, as such, was authorized to take actions necessary with respect to the management and operation of Company A.

Effective Date 2, 2000, Company B acquired the assets and accounts of Company A.

On Date 3, 2001, Court F, which had jurisdiction over Company A's receivership, entered a final order with respect to the Sum 1 short-fall referenced above.

The Date 3, 2001, Court Order (Order), provided, in relevant part, that a short-fall of approximately Sum 1 existed in the cash trust assets of Company A. Furthermore, the Order indicated that Company A is unable to meet its obligations to its account holders, that it is not feasible or possible to trace the misappropriation of the cash trust funds to specific Company A accounts, and that an allocation of the Sum 1 short-fall to Company A accounts must be made.

The Order further indicates that Company B, as the successor trustee to Company A, is responsible for collecting and implementing the Sum 1 short-fall from the affected trust accounts.

Additionally, the Order provides that Company B shall offer to the holder of each affected account a choice of options for collecting the amount allocated to each holder's account. One of the choices given an affected account holder is for that account holder to pay Company B the amount allocated against his account from assets outside of the account, which assets may be provided by third parties. Any account holder who chooses this option will not have his or her account, including an IRA, debited in the amount of the allocation.

Finally, the Order provides that after an allocated amount is collected from an affected IRA account holder, Company D, as receiver, shall record on the books of Company A a claim by the payor thereof in the sum of the allocated amount. In addition, the receiver shall issue to the payor of the allocated amount, a "Receivership Certificate" in the amount that equals the allocated amount. Your authorized representative asserts that if an account holder who pays his allocated amount with assets other than his account assets is entitled to reimbursement, by reason of his holding a "receivership certificate", any amounts reimbursed shall be paid directly to the account holder and shall not be contributed to his or her account including an IRA.

Taxpayer C holds an IRA with Company B. His IRA has been allocated a short-fall amount in accordance with the Date 3, 2001, Court Order. Taxpayer C has chosen to pay the amount of his allocation from assets outside of his IRA which assets may be provided to Taxpayer C by a third party.

Based on the above facts and representations, you, through your authorized representative, request the following letter rulings:

1. If an affected IRA account holder pays the short-fall amount allocated to his account directly to Company B with assets other than from his or her account, including assets provided by a third party, then said payment will:
   a. not constitute a contribution or payment to the IRA subject to the limitations on contributions found in Code section 219;
   b. not constitute a distribution from the IRA taxable in accordance with Code section 408(d);
   c. will not be subject to the excise tax described in Code section 4973; and
   d. need not be reported on Form 5498.

2. If amounts are later recovered and an affected IRA account holder is reimbursed for any part of the short-fall allocation he or she paid with assets outside of amounts held in his or her account, which reimbursement will not be contributed to his or her IRA, then such reimbursement shall:

   a. not be treated as a contribution subject to the limitations of Code section 219;
   b. not be subject to the tax imposed by Code section 4973; and
   c. not be subject to the reporting requirements applicable to IRAs, including, but not limited to, reporting on a Form 1099-R.

With respect to your ruling requests, Code section 219(a) provides that a deduction may be taken for a contribution to an IRA in the amount of the qualified retirement contribution of an individual for a taxable year. Code section 219(b) limits the maximum deductible contribution to an individual for a taxable year to the lesser of (A) $2000 or (B) the compensation includible in the individual's gross income for the taxable year.

Code section 408(a) sets forth the requirements which must be met by an IRA. One of the requirements, set forth in Code section 408(a)(1), is that the written instrument governing the IRA must provide that no contribution, other than a rollover contribution, will be accepted for any taxable year in excess of $2000 on behalf of any individual.

Code section 408(d)(1) provides, in short, that any amount paid or distributed from an individual retirement plan shall be included in gross income by the payee or distributee, as the case may be, in the manner provided under section 72.

Code section 4973(a) provides, in short, for the imposition of a tax in the amount of six percent of the amount of any excess contribution made to a individual retirement account described in Code section 408(a) or individual retirement annuity described in Code section 408(b).

Form 5498, IRA Contribution Information, is used by the trustee or issuer of an IRA to report contributions and the fair market value of an individual retirement account to the Internal Revenue Service.

Form 1099-R, Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc., is used by plans, IRAs etc. to report distributions therefrom to recipients thereof.

The Code sections and Forms, referenced above, either provide guidance or are used to provide information relative to distributions from and contributions to qualified plans and IRAs. The ruling requests made by you concern the amounts that will either be paid by or reimbursed to the payor from sources other than plan or IRA amounts.

Revenue Ruling 84-146, 1984-2 C.B. 61, discusses the deductibility of trustees' fees with respect to IRAs. It holds that, consistent with the rules governing deductions in connection with qualified plans, amounts paid by the IRA owner for such fees in connection with an IRA are deductible under section 212 of the Code to the extent they satisfy the requirements of that section, but amounts paid that are not ordinary and necessary expenses, such as capital expenditures and disguised IRA contributions, are not deductible under section 212.

Revenue Ruling 86-142, 1986-2 C.B. 60, provides that brokers' commissions incurred in investments for qualified plans and IRAs, paid directly to the broker or paid to the trust as reimbursement for commissions paid by the trust, are treated as though they were contributed to the trust and used to provide benefits under the plan. Such payments are not deductible under either section 162 or section 212 of the Code. Rather, these contributions (and payments treated as IRA contributions) are deductible subject to the limits of section 219.

In this case, Taxpayer C, and others similarly situated, either have had or will have their IRA accounts allocated a portion of the Sum 1 short-fall referenced in the Order. However, Taxpayer C and other, similarly situated, taxpayers will pay said allocations directly to Company B from non-IRA assets. The Service is of the opinion that it is consistent with the principles set forth in the two revenue rulings referenced above to hold that the facts outlined above describe both a contribution as that term is used in Code section 219, Code section 4973(a) and Form 5498, and a distribution as that term is used in Code section 408(d)(1) and Form 1099-R. Since Taxpayer C and similarly situated IRA owners have the option of having their IRAs debited with the amount(s) of their allocations, and if they choose the option referenced above their IRAs will not be debited in the amount(s) of their allocations, it is appropriate to treat the transaction as if Taxpayer C, and other similarly situated taxpayers, had initially contributed the allocated amount(s) to their IRAs which then distributes said allocated amounts to Company B. Furthermore, if reimbursement is made, the reimbursed amounts will be treated as if they are initially contributed to the IRAs of Taxpayer C and other, similarly situated, affected IRA holders which then distributes said reimbursed amounts to the owners of said IRAs.

Thus, with respect to your ruling requests, the Service concludes as follows:

1. If an affected IRA account holder pays the amount allocated to his or her IRA account directly to Company B, then said payment, will:

   a. constitute a contribution or payment to the IRA subject to the limitations on contributions found in Code section 219;
   b. constitute a distribution from the IRA taxable in accordance with Code section 408(d) when paid to Company B;
   c. will be subject to the excise tax described in Code section 4973; and
   d. need to be reported on Form 5498.

2. If amounts are later recovered and an affected IRA account holder is reimbursed for any part of the allocation he or she paid with assets outside of amounts held in his or her account, which reimbursement will not be contributed to his or her IRA, then such reimbursement shall:

   a. be treated as a contribution subject to the limitations of Code section 219;
   b. be subject to the tax imposed by Code section 4973; and
   c. be subject to the reporting requirements applicable to IRAs, including, but not limited to, reporting on a Form 1099-R.

The above rulings are based on the facts represented herein. Furthermore, please note that the conclusions of this letter ruling apply even if the source of the amounts paid to Company B is a third party provider.

This letter is directed only to the taxpayers that requested it. Section 6110(j)(3) of the Code provides that it may not be used or cited as precedent.

200151051

Pursuant to a power of attorney on file with this office, a copy of this ruling letter is being sent to your authorized representative.

Sincerely yours,

Frances V. Sloan

Frances V. Sloan
Manager, Employee Plans
Technical Group 3
Tax Exempt and Government
Entities Division

Enclosures:

Deleted copy of ruling letter
Notice of Intention to Disclose

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