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DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

200418051

FEB 04 2004

T:EP:RA:T1

Attention:

Legend

Employer A = ***

Country C = ***

Country D = ***

Agency E = ***

State F = ***

State G = ***

Province H = ***

Plan W = ***

Plan X = ***

Plan Y = ***

Plan Z = ***

Ladies and Gentlemen:

This is in response to a letter dated June 24, 2002, as supplemented by correspondence dated July 23, 2002, August 7, 2002, January 14, 2003, December 19, 2003 and January 7, 2004, submitted on your behalf by your authorized representative, in which you request a private letter ruling dealing with the spin-off of a portion of a retirement plan qualified under section 401(a) of the Internal Revenue Code (the "Code"), to a plan with a trust maintained in Country C. The following facts and representations have been submitted:

Employer A is a corporation established under the laws of State F, with its principal office located in State G. Employer A maintains additional offices in other locations in the United States, as well as a branch office in Country C.

Employer A maintains Plan X, a defined benefit pension plan that meets the requirements of section 401(a) of the Code. Plan X currently benefits a small minority of participants who are employed at Employer A's branch office in Country C, and Plan X also benefits two retirees who are receiving benefits and are residents of Country C (collectively the "Country C Participants").

The Country C Participants are nonresident aliens within the meaning of section 7701(b)(1)(B) of the Code, and are non highly compensated employees within the meaning of Code section 414(q). Plan X does benefit one highly compensated employee who works in the branch office in Country C, and is a citizen of Country D, and a lawful permanent resident of the United States. Unlike the Country C Participants, the one highly compensated employee who works in Country C is not considered as having his permanent principal place of employment in Country C. Thus, this employee is a resident alien within the meaning of section 7701(b)(1)(A) of the Code. The most recent favorable determination letter with respect to Plan X is dated April 12, 2002.

Since its establishment in . Plan X has never had an accumulated funding deficiency. Plan X has covered all eligible employees of Employer A without regard to where the employee lives and works. Employer A asserts that it has recently been advised that the accrual of benefits under a plan intended to meet the requirements of section 401(a) of the Code, that does not satisfy the requirements of the federal and provincial laws of Country C, could represent a taxable event for the Country C Participants, and could adversely affect their ability to contribute to a registered retirement plan in Country C.

In an effort to alleviate adverse Country C tax consequences to the Country C Participants, and to comply with Country C legislation, Employer A established Plan Y, in Country C, effective . Plan Y is a registered plan under

the federal and provincial laws of Country C. In connection with the establishment of Plan Y, the restatement of Plan X, adopted on , provides that an employee whose permanent principal place of employment is outside the United States is not eligible to participate in Plan X after , and that no benefits will accrue for Country C Participants after that date.

Plan Y covers the Country C Participants as well as all other employees of Employer A whose permanent principal place of employment is in Country C, and who satisfy Plan Y's eligibility requirements (which are identical to those of Plan X). Plan Y provides future benefit accruals equal to the accruals that would have occurred under Plan X. In addition, subject to the transfer of assets with respect to which this ruling request is made, Plan Y will provide each Country C Participant who was employed by Employer A on , with a past service benefit as of equal to his or her accrued benefit under Plan X as of that date. Following the transfer of assets to Plan Y, Plan Y will pay the benefits of the two retirees residing in Country C that are currently being paid by Plan X.

In connection with the transfer of assets and liabilities from Plan X to Plan Y, and solely for the purpose of facilitating that transfer, Employer A will establish Plan Z. Plan Z will be a defined benefit pension plan, the terms of which will be identical to Plan X, except that participation in this plan will be limited to the Country C Participants. Consequently, Plan Z will benefit solely citizens and residents of Country C. Plan Z will contain provisions intended to comply with the requirements of section 401(a) of the Code, including language to the effect that the assets of Plan Z must be used for the exclusive benefit of participants in the plan and their beneficiaries.

Following the establishment of Plan Z, Employer A will spin off to Plan Z the portion of Plan X that benefits the Country C Participants. Under the spin-off, all of the benefits of the Country C Participants will be spun off to Plan Z, and all of the benefits of the other participants will remain in Plan X.

Because the assets of Plan X are insufficient to provide for the payment for all liabilities of Plan X, the value of the assets to be spun off to Plan Z will be determined by allocating the assets of Plan X to priority categories in accordance with section 4044 of the Employee Retirement Income Security Act of 1974 (ERISA). This allocation will be made as of the date on which the amendment to Plan X providing for the transfer of assets is adopted and the present value of accrued benefits for purposes of this allocation will be determined as of that date, using the applicable interest rate as defined in section 417(e)(3) of the Code for the preceding month, and the applicable mortality table, as also defined in

section 417(e)(3). The amount to be transferred to Plan Z will be the amount thus determined. The assets so transferred will be held either in a Country C trust established in connection with Plan Z, or one or more insurance contracts in accordance with the applicable provincial law of Country C.

Under the terms of Plan Z, each Country C Participant will be entitled to receive benefits on a termination basis, as defined in section 1.414(l)-1(b)(5) of the Income Tax Regulations (the "regulations"), under that plan immediately after the transfer of assets and liabilities that are equal to or greater than the benefits the participant would have received on a termination basis under Plan X immediately before the transfer. Similarly, each participant in Plan X with respect to whom no transfer is made to Plan Z will be entitled to receive benefits on a termination basis under Plan X immediately after the transfer of assets and liabilities that are equal to or greater than the benefits the participant would have received on a termination basis immediately before the transfer.

An application will be made on behalf of Employer A to Agency E for a special ministerial waiver under Country C's Income Tax Act to permit the transfer of pension assets from Plan X to Plan Y. Subject to the receipt of that waiver and the rulings requested in this letter, Employer A will cause Plan X to transfer a portion of the assets and liabilities of Plan X to Plan Z. Plan Z will then be amended as necessary to comply with both the Pension Benefits Act of Province H and the Income Tax Act of Country C, and will be restated as Plan W and merged in Country C into Plan Y. The amount of the liabilities transferred to Plan Z will equal all of the liabilities of Plan X related to the Country C Participants. No assets will be transferred with respect to the one highly compensated employee employed in Country C who currently participates in Plan X.

The above amendment to Plan Z may result in Plan Z not satisfying the requirements of section 401(a) of the Code. As a result of the amendment, Plan Z will instead be qualified, funded and operated in compliance with the federal and provincial law of Country C, and will not be subject to Titles I and IV of ERISA, or the jurisdiction of the Internal Revenue Service (the "Service"). The provision in Plan Z to the effect that the assets of Plan Z must be used for the exclusive benefit of the participants in that plan and their beneficiaries will remain in Plan Z after its restatement as Plan W, and is repeated in Plan Y.

Plan Y will be qualified, funded and operated in compliance with the Pension Benefits Act of Province H and the Income Tax Act of Country C. Plan Y will not be subject to Titles I and IV of ERISA, nor will it be subject to the jurisdiction of the Service. Plan Y will, as previously represented, provide that the assets of Plan Y must be used for the exclusive benefit of its participants and their beneficiaries.

Employer A asserts that Country C and Province H, either by statute or through case law, impose requirements on pension plan administrators, and afford pension plan participants protections similar to, and in certain cases greater than, those imposed in the United States, including requirements on plan administrators similar to the provisions of section 401(a)(2) of the Code.

Benefits under Plan Y, including amounts transferred from Plan X to Plan Y through Plan Z (which will be restated as Plan W and merged in Country C into Plan Y), will be made available or distributed to the Country C Participants solely in accordance with the applicable provisions of Plan Y and the laws of Country C and Province H. Plan Y will not satisfy all of the requirements of section 401(a) of the Code. Consequently, while Employer A will make recurring future contributions to Plan Y to fund benefits for the Country C Participants and other participants in that plan, such contributions will not be deductible under section 404 of the Code, but may be deductible under section 404A of the Code.
Based upon the foregoing, the following rulings are requested:

1. That spinning off the portion of Plan X that benefits the Country C Participants to Plan Z, transferring a portion of the assets held in Plan X's trust to a trust or insurance contract for Plan Z maintained in Country C, and amending Plan Z as noted above, which actions, it is represented, will result in Plan Z no longer being subject to Titles I and IV of ERISA and no longer satisfying section 401(a) of the Code, will not cause Plan X to violate the exclusive benefit rule of Code section 401(a)(2).

2. That transferring a portion of the assets and liabilities of Plan X to a trust or insurance contract maintained for Plan Z in Country C, where it is represented that Plan Z will not be subject to Titles I and IV of ERISA and will not satisfy Code section 401(a), will not result in distributions to the Plan Z participants (the Country C Participants).

3. That transferring a portion of the assets held in Plan X's trust sufficient to satisfy Plan Z's obligations to its participants, to a trust or insurance contract maintained for Plan Z in Country C will not cause Plan Z to violate the minimum funding requirements of section 412 of the Code.

With respect to ruling request 1, section 401(a)(2) of the Code provides that a plan will not be qualified under Code section 401(a) unless "if under the trust instrument it is impossible, at any time prior to the satisfaction of all liabilities with respect to employees and their beneficiaries under the trust, for any part of the corpus or income to be . . . used for, or diverted to, purposes other than for the exclusive benefit of the employees or their beneficiaries."

Section 1.401-2(a)(3) of the regulations provides that the term "purposes other than for the exclusive benefit of the employees or their beneficiaries" means "all objects or aims not solely designed for the proper satisfaction of all liabilities to employees or their beneficiaries covered by the trust."

Section 4(b) of ERISA provides, in part, that the provisions of this title (Title I) shall not apply to any employee benefit plan if such plan is maintained outside of the United States primarily for the benefit of persons substantially all of whom are nonresident aliens.

Section 4021(a) of ERISA lists the types of plans to which Title IV applies. Section 4021(b) of ERISA provides, in part, that this section does not apply to any plan which is established and maintained outside of the United States primarily for the benefit of individuals substantially all of whom are nonresident aliens.

In this case, the participants in Plan Z will be the Country C Participants who are citizens and residents of Country C, and are currently entitled to benefits under Plan X. After the spin off, these individuals will be entitled to benefits under Plan Z, and the assets transferred to Plan Z will consist of a portion of the assets currently held under Plan X to provide benefits to current Plan X participants. Thus, after the spin off, all of the assets held in Plan X's trust prior to the spin off will be used for the benefit of participants of Plans X and Z and their beneficiaries.

Furthermore, after Employer A begins to maintain Plan Z, the assets that are spun off from Plan X will be transferred to an investment vehicle maintained in Country C in connection with Plan Z. As a result, the assets of Plan Z will continue to be used to provide benefits for Plan Z participants.

In summation, the assets presently held in Plan X's trust, which represent contributions to Plan X and net investment gains with respect thereto, will be used to provide benefits for those individuals who presently participate, or have participated, in Plan X. After the spin off to Plan Z from Plan X, a portion of the assets held in Plan X's trust will have been transferred to an investment vehicle maintained in Country C in connection with Plan Z for the benefit of Plan Z participants.

Therefore, based on these particular facts and circumstances, we conclude with respect to ruling request 1 that spinning off the portion of Plan X that benefits the Country C Participants to Plan Z which is maintained by Employer A, and transferring a portion of the assets held in Plan X's trust to a trust or insurance contract for Plan Z maintained in Country C, and amending Plan Z as noted above, as a result of which it is represented that Plan Z will no longer be subject

to Titles I and IV of ERISA and will not satisfy section 401(a) of the Code, will not cause Plan X to violate the exclusive benefit rule of section 401(a)(2) of the Code.

With respect to ruling request 2, Code section 402(a)(1) provides that, "except as otherwise provided in this section, any amount actually distributed to any distributee by any employees' trust described in section 401(a) which is exempt from tax under section 501(a) shall be taxable to the distributee, in the taxable year of the distributee in which distributed, under section 72 (relating to annuities)."

Code section 402(d) provides that, "For purposes of subsections (a), (b), and (c), a stock bonus, pension, or profit-sharing trust which would qualify for exemption from tax under section 501(a) except for the fact that it is a trust created or organized outside the United States shall be treated as if it were a trust exempt from tax under section 501(a)."

Code section 404(a)(4) provides that "If a stock bonus, pension, or profit-sharing trust would qualify for exemption under section 501(a) except for the fact that it is a trust created or organized outside the United States, contributions to such a trust by an employer which is a resident, or corporation, or other entity of the United States, shall be deductible under the preceding paragraphs" (relating to the deduction of contributions to plans with trusts which are tax-exempt under section 501(a)).

Code section 402(b)(1) provides, in relevant part, that contributions to an employees' trust made by an employer during a taxable year of the employer which ends with or within a taxable year of the trust for which the trust is not exempt shall be included in the gross income of the employee in accordance with section 83.

Code section 402(b)(2), provides, generally, that amounts distributed or made available to any distributee by a nonexempt trust shall be taxable in the year so distributed or made available under Code section 72.

In this case, Plan Z will be spun off from Plan X. Plan Z will be maintained by Employer A, and the assets transferred to Plan Z will be transferred to an investment vehicle maintained in Country C in connection with Plan Z. The transfer of assets will be from a trust created and maintained in the United States to a trust or insurance contract maintained for Plan Z in Country C. In effect, as a result of the transactions described herein, a portion of the assets currently held

in trust for Plan X participants will be transferred to Plan Z, where they will continue to be held in trust for certain of the current Plan X participants who will become participants in Plan Z (the Country C Participants).

Furthermore, as noted above, Employer A asserts that benefits under Plan Y, including amounts transferred from Plan X to Plan Y through Plan Z (which will be restated as Plan W and merged in Country C into Plan Y), will be made available or distributed to the Country C Participants solely in accordance with the terms of Plan Y and, when applicable, in accordance with the laws of Country C and Province H.

Under the facts presented in this case, no distribution, as that term is defined for purposes of section 402 of the Code, will be made from Plan Z to any of its participants as a result of either the spin-off, referenced herein, Employer A maintaining Plan Z, or the transfer of a portion of Plan X's assets, held in trust in the United States, to a trust or insurance contract maintained for Plan Z in Country C.

Therefore, with respect to ruling request 2, we conclude that having Plan Z maintained by Employer A, and transferring a portion of Plan X assets to a trust or insurance contract maintained for Plan Z in Country C, where, it is represented, Plan Z will not be subject to Titles I and IV of ERISA, and will not satisfy Code section 401(a), will not result in distributions to participants of Plan Z (the Country C Participants).

With respect to ruling request 3, section 412 of the Code provides the minimum funding standards for qualified pension plans.

Section 412(a) provides that the minimum funding standards apply "to a plan if, for any plan year beginning on or after the effective date of this section for such plan," the plan included a trust which qualified under section 401(a). Furthermore, "a plan to which this section applies shall have satisfied the minimum funding standard for such plan for a plan year if as of the end of such plan year, the plan does not have an accumulated funding deficiency." An accumulated funding deficiency is defined as the excess of total charges to the funding standard account for all plan years to which section 412 applies, over the total credits for all such plan years.

Revenue Ruling 81-212, 1981-2 C.B. 99, provides rules for splitting the funding standard account of a defined benefit plan to reflect a spinoff of assets and liabilities from the plan.

Section 4(b) of ERISA provides that the provisions of Title I of ERISA do not apply to any employee benefit plan that is maintained outside of the United States primarily for the benefit of persons substantially all of whom are nonresident aliens. Section 4021(b) of ERISA provides that section 4021 of ERISA does not apply to any plan that is established and maintained outside of the United States primarily for the benefit of individuals substantially all of whom are nonresident aliens.

In accordance with Rev. Rul. 81-212, because Plan X has never had an accumulated funding deficiency, Plan Z will also not have an accumulated funding deficiency immediately after the spin-off.

In substance, the proposed transaction involves a transfer of assets and liabilities from Plan X to Plan Z which is characterized as a spinoff from Plan X to Plan Z. Such characterization is required under Code section 414(l) for purposes of determining whether the transfer satisfies the qualification requirements of that section. Although such characterization is required, based on the authority cited above, and based on the representation that Plan Z will solely benefit citizens and residents of Country C who are nonresident aliens within the meaning of Code section 7701(b)(1)(B), no additional minimum funding requirements under section 412 would accrue for the spunoff Plan Z.

Therefore, with respect to ruling request 3, we conclude that transferring a portion of the assets held in Plan X's trust sufficient to satisfy Plan Z's obligations to its participants, to a trust or insurance contract maintained for Plan Z in Country C will not cause Plan Z to violate the minimum funding requirements of section 412 of the Code.

This letter ruling is based on the assumption that Plan X is qualified under Code section 401(a) at all times relevant thereto. It also assumes that the transfer of assets and liabilities from Plan X to Plan Z will comply with section 414(l) of the Code.

This letter ruling addresses issues raised under the Code. It does not address issues raised under Title I of ERISA, nor does it address the effect, if any, which the Convention between the United States and Country C with respect to taxes on income and on capital has on the transaction(s) described herein. Specifically, it does not address the issue of whether the transaction(s) described herein will give rise to distributions to Country C citizens under the laws of Country C.

A copy of this ruling is being sent to your authorized representative pursuant to a power of attorney on file in this office. Should you have any questions pertaining to this ruling, you may contact *** of this office at ***.

Sincerely yours,

Carlton Watkins

Carlton Watkins, Manager
Employee Plans Technical Group 1

Enclosures:
Deleted Copy of the Ruling Letter
Notice of Intention to Disclose, Notice 437

cc: