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**Internal Revenue Service**

Department of the Treasury

Significant Index No. 0412.07-00

Washington, DC 20224

Person to Contact:

Telephone Number:

Refer Reply to: T:EP:RA:T:A1

Date: SEP 11 2000

In re:

Employer =

Parent =

This letter constitutes notice that with respect to the above-named money purchase pension plan we have denied approval for the plan amendment dated March 30, 2000 that would have retroactively amended the plan so as to reduce accrued benefits.

Section 411(d)(6) of the Internal Revenue Code and § 204(g) of the Employee Retirement Income Security Act of 1974 (ERISA) prohibit a plan amendment, except for an amendment described in Code § 412(c)(8) and ERISA § 302(c)(8), that has the effect of decreasing a participant's accrued benefit under the plan.

Code § 412(c)(8) and ERISA § 302(c)(8) provide that any amendment applying to a plan year which (1) is adopted no later than 2 1/2 months after the close of such plan year, (2) does not reduce the accrued benefit of any participant determined as of the beginning of the first plan year to which the amendment applies, and (3) does not reduce the accrued benefit of any participant determined as of the time of the adoption except to the extent required by the circumstances, shall, at the election of the plan administrator, be deemed to have been made on the first day of such plan year. No such amendment which reduces the accrued benefits of any participant shall take effect unless the plan administrator files a notice with the Secretary of Labor notifying him of such amendment and the Secretary of Labor has approved such amendment, or within 90 days after the date on which such notice was filed, failed to disapprove such amendment.

Code § 412(c)(8) and ERISA § 302(c)(8) also provide that no amendment which reduces the accrued benefits of plan participants shall be approved unless it is determined that (1) such amendment is necessary because of substantial business hardship as determined under Code § 412(d)(2) and ERISA § 303, and (2) a waiver of the minimum funding standard is unavailable or inadequate. Reorganization Plan No. 4 that became effective December 31, 1978, transferred the authority of the Secretary of Labor under Code § 412(c)(8) and ERISA § 302(c)(8) to the Secretary of the Treasury.

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Code § 412(d) provides for a waiver of the minimum funding standard if an employer has experienced temporary substantial business hardship. Code § 412(d)(2) provides that the factors taken into account in determining temporary substantial business hardship shall include (but shall not be limited to) whether or not:

(1) The employer is operating at an economic loss,

(2) There is substantial unemployment or underemployment in the trade or business and in the industry concerned,

(3) The sales and profits of the industry concerned are depressed or declining, and

(4) It is reasonable to expect that the plan will be continued only if the waiver is granted.

The Employer is part of a controlled group and manufactures containing one or more and associated Typically, these are used for workstations. The Parent's main business is development. From the material submitted, the Parent was profitable through 1997. In that same year the Parent purchased the Employer.

The Plan covers 95 participants. Prior to the amendment in question, the Plan provided for a contribution equal to 3 percent of each participant's compensation. The amendment would cease benefit accruals as of January 1, 1999. The cost savings to the Employer from the amendment would be approximately $220,963.

As stated above, Code § 412(c)(8) requires that a retroactive amendment to reduce benefits must be adopted no later than 2-1/2 months after the end of the plan year. The plan year in question is the 1999 calendar year. Therefore, in order for the Service to consider approving a retroactive plan amendment reducing plan benefits, the sponsor must adopt such an amendment no later than March 15, 2000. The amendment in question was not adopted timely as it was adopted on March 30, 2000 - 15 days after the statutory deadline.

In considering the request for approval of the retroactive amendment, we must consider the factors set forth in Code § 412(d)(2) as they apply in the context of a request for a reduction of accrued benefits under Code § 412(c)(8). Other factors may be considered as well. The first factor considered was whether the Employer was operating at an economic loss. In 1998, the controlled group experienced net losses. Taking into account the purchases of the Employer and two other companies, sales increased by 83 percent. However, the group had a loss of $2.1 million and working capital went from positive $3.5 million in 1997 to negative $3.6 million in 1998. Net worth remained positive but declined by 11 percent.

In 1999, the controlled group continued to have economic hardship as evidenced by a net loss of $11.2 million on gross sales of $35.2 million. The group also had negative working capital ($10 million). Net worth remained positive but declined by 64 percent from 1998.

The controlled group's line of credit has been revoked. The Parent has also received a letter from its lender requesting payment in full. The Employer has reduced staff by half. Further reductions are expected.

The second factor under Code § 412(d)(2) concerns unemployment or underemployment in the Employer's trade or business. The controlled group has two operating lines: (1) its original development business and (2) the business of the Employer. No other information has been provided regarding whether there is substantial unemployment or underemployment in the development business. The Employer has stated that in some businesses similar in size and nature to itself the number of employees has decreased by 13 percent from 1998 to 1999. No additional information illustrating unemployment or underemployment was provided.

The third factor under Code § 412(d)(2) concerns sales and profits of the Employer's "industry". No information has been sent illustrating whether there are declining profits in the development business. The Employer stated that sales in the industry grew 29 percent in 1999. No additional information concerning sales and profits in the "industry" was provided.

The fourth factor under Code § 412(d)(2) concerns whether it is reasonable to expect the Plan to be continued only if the amendment is approved. The Employer states that in order to survive it needs to reduce costs wherever possible. The amendment would save the controlled group a $220,963 contribution to the Plan - an amount equal to 4 percent of the Employer's gross profit. Contributions for the 2000 plan year have been frozen. The controlled group has no line of credit, no asset-based loan and working capital is worse. The Employer has no available cash on hand. The Parent has received a letter from its lender requesting payment in full.

Given that the Plan is a money purchase plan and allocations will cease beginning in 2000, it is not clear that the Plan can continue only if the amendment is approved. The Employer has not advanced any argument as to why that is the case. Costs for the Plan for future years have already been reduced. It has not been demonstrated that removal of the 1999 costs for the Plan is critical to the survival of the Plan. In fact, the amount at issue is a relatively small part of the overall finances of the Employer. The savings from the amendment amount to less than 4 percent of gross profit. Therefore, it seems unlikely that the savings from the amendment would have much of an impact on the continuation of the Plan.

Another factor to consider is that the Service has received comments from Plan participants. The participants are unanimous in asking the Service to deny the Employer's request for approval of the proposed amendment.

Because the amendments would reduce accrued benefits as of the date of adoption, we must consider whether a funding waiver is unavailable or inadequate. A funding waiver could have been requested. The Employer has substantial business hardship. Therefore, a waiver may have been available. We would have to determine whether the business hardship is temporary.

Also, it appears that a waiver of the minimum funding standard would be adequate. A waiver of the minimum funding standard for the plan year ended December 31, 1999 would eliminate costs for 1999. If a waiver for the 1999 plan year were granted, the annual amortization amount for a waiver of $220,963 would be approximately $55,000. The Employer has stated that it has adopted an amendment, effective January 1, 2000, that freezes further contributions. Therefore, the annual amount needed to satisfy the minimum funding standard over the next five years would be solely the amortization payment (i.e., $55,000). The financial reports indicate that neither the Employer nor the controlled group has any available cash on hand.

The lack of cash for both the Employer and the controlled group brings up the question as to whether a waiver of the minimum funding standard would be adequate. It is not clear as to whether the additional cost of amortizing a waiver would have a material effect on the Employer's finances or the controlled group's finances over the next five (5) years.

On July 26, 2000 and again on August 24, 2000, we informed you via telephone of our tentative denial and your right to a conference. In a letter dated September 1, 2000, we stated that such a conference needed to be scheduled by September 11, 2000. No additional material has been furnished.

The amendment was executed after the 2-1/2 months permitted by law. The Employer and the controlled group are operating at a loss - but the Employer has not presented a viable recovery plan. The Employer has not expressed an expectation of when contributions would resume. The information sent to us indicates that there is not substantial unemployment or underemployment in either the development industries. Contrary to declining sales, the industry is experiencing a growth in sales. As for whether the amendment is needed in order for the plan to continue, the Employer does not indicate if future contributions to the Plan will resume even if the amendment is approved. Also, a substantial number of plan participants have written to the Service asking not to take away the contributions they feel they are entitled to.

Therefore, based on the failure to timely adopt the amendment and on the information submitted, the request for approval of the retroactive amendment has been denied.

Sincerely,

Richard A. Uhrig

for Carol D. Gold, Director
Employee Plans
Tax Exempt and Government Entities
Division