Doing v. Commissioner, 58 T. C. 115 (1972)

A transfer of funds between two qualified retirement plans does not constitute a premature distribution if the funds are not used for personal benefit and the transfer is part of a plan amendment.

Summary

Keith Doing, a veterinarian, sought to amend his self-employment retirement plan by transferring funds from Financial Industrial Fund (FIF) to Keystone Custodian Funds without tax consequences. Despite his instructions, the initial custodian, First National Bank, sent the funds directly to Doing, who immediately forwarded them to Keystone. The U. S. Tax Court ruled that this transfer did not constitute a premature distribution under IRC Sec. 72(m)(5)(A)(i) because Doing did not intend to terminate his plan or use the funds personally. The court emphasized the substance of the transaction, allowing Doing to avoid a 110% tax penalty and continue contributing to his retirement plan in subsequent years.

Facts

Keith Doing, a self-employed veterinarian, established a self-employment profit-sharing retirement plan with Financial Industrial Fund (FIF) in 1964, administered by First National Bank of Denver as custodian. In 1966, upon advice from his investment counselor, Doing decided to change the investment medium from FIF to Keystone Custodian Funds, managed by New England Merchants National Bank. Doing executed the necessary applications for the new plan and requested First National to liquidate his shares in the FIF plan and send the proceeds directly to Keystone. However, First National sent the proceeds to Doing instead, requiring him to endorse and forward the check to Keystone, which he did promptly. Both plans were qualified under IRC Sec. 401.

Procedural History

The Commissioner of Internal Revenue determined deficiencies in Doing's federal income tax for 1966 and 1967, asserting that the funds received from First National constituted a premature distribution under IRC Sec. 72(m)(5)(A)(i), subjecting Doing to a 110% tax penalty and disallowing his 1967 retirement plan contributions under IRC Sec. 401(d)(5)(C). Doing petitioned the U. S. Tax Court, which ultimately ruled in his favor, finding no premature distribution occurred and allowing his subsequent retirement plan contributions.

Issue(s)

1. Whether the funds received by Doing from First National constituted a premature distribution under IRC Sec. 72(m)(5)(A)(i), subjecting him to a 110% tax penalty under IRC Sec. 72(m)(5)(C)?
2. If a premature distribution occurred, whether Doing's deduction for contributions

to a self-employment retirement plan in 1967 was prohibited by IRC Sec. 401(d)(5)(C)?

Holding

1. No, because the funds were immediately transferred to another qualified plan without personal use, consistent with Doing's intent to amend his retirement plan rather than terminate it.
2. No, because no premature distribution occurred, Doing was not barred from claiming a deduction for contributions to a self-employment retirement plan in 1967.

Court's Reasoning

The court focused on the substance of Doing's transaction, noting that he intended to amend his plan to change investment mediums rather than terminate it or withdraw funds. The court rejected the Commissioner's argument that the transfer to Doing constituted a premature distribution, emphasizing that Doing took immediate corrective action to forward the funds to Keystone. The court cited IRS regulations and revenue rulings indicating that a change in funding medium or custodian does not necessarily result in a distribution if the funds are transferred between qualified plans. The court also considered the legislative intent behind IRC Sec. 72(m)(5), which aims to prevent the use of retirement plans for income averaging, not to penalize legitimate plan amendments. The court noted that the error by First National should not control the tax consequences when Doing's actions were consistent with proper plan amendment procedures.

Practical Implications

This decision clarifies that transferring funds between qualified retirement plans as part of a plan amendment does not constitute a premature distribution if the funds are not used for personal benefit. It allows taxpayers to change investment options within their retirement plans without tax penalties, provided the transfer is executed properly. The ruling emphasizes the importance of documenting intent to amend rather than terminate a plan and taking immediate corrective action if errors occur. Practitioners should advise clients to ensure clear communication with custodians and to promptly rectify any mistakes to avoid unintended tax consequences. Subsequent cases, such as Rev. Rul. 71-541, have cited Doing in support of similar transfers between qualified plans.

