Oakton Distributors, Inc. v. Commissioner, 73 T. C. 182 (1979)

Retroactive amendments to disqualifying provisions in pension and profit-sharing plans are not permitted if made after the expiration of the remedial amendment period without a timely request for extension.

Summary

Oakton Distributors, Inc. established a money purchase pension plan in 1970 and a profit-sharing plan in 1972, both integrated with Social Security. The IRS issued favorable determination letters for both plans but later revoked the profit-sharing plan's qualification due to excessive integration when combined with the pension plan. The company attempted to retroactively amend the profit-sharing plan over three years after the initial determination. The Tax Court held that such amendments were not permissible because they were made after the remedial amendment period had expired and no timely extension request was filed. The court also upheld the retroactive revocation of the plan's qualified status due to a misstatement of material facts in the original application.

Facts

In 1970, Oakton Distributors, Inc. adopted a money purchase pension plan integrated with Social Security to the maximum extent allowed, receiving a favorable determination letter from the IRS. In December 1972, the company adopted a profit-sharing plan also integrated with Social Security, covering the same employees as the pension plan. The profit-sharing plan's application misstated the pension plan's contribution formula, leading to a favorable determination letter in March 1973. In 1976, the company sought determination that the profit-sharing plan, amended to comply with ERISA, continued to qualify. The IRS then discovered the excessive integration and revoked the profit-sharing plan's qualification retroactively to 1972.

Procedural History

The IRS issued a favorable determination letter for the pension plan in 1970 and for the profit-sharing plan in 1973. In 1976, after reviewing the ERISA compliance application, the IRS discovered the excessive integration and issued a final adverse determination letter in August 1977, retroactively revoking the profit-sharing plan's qualification to 1972. Oakton Distributors, Inc. challenged this revocation in the U. S. Tax Court, which upheld the IRS's decision.

Issue(s)

1. Whether a profit-sharing plan adopted in 1972 and determined qualified in 1973 can be retroactively amended in 1977 to remove a disqualifying provision.
2. Whether the IRS abused its discretion by retroactively revoking the prior favorable determination letter for the profit-sharing plan.

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Holding

1. No, because the company did not request an extension of the remedial amendment period before it expired, and the proposed amendment was made more than three years after the initial determination, which was not considered reasonable under the circumstances.
2. No, because the company misstated a material fact in its initial application for the profit-sharing plan, justifying the retroactive revocation.

Court’s Reasoning

The court applied section 401(b) of the Internal Revenue Code and related regulations, which allow retroactive amendments during a defined remedial amendment period. Oakton’s attempt to amend the plan in 1977 was well beyond the remedial amendment period, which ended in July 1973, and no timely extension request was made. The court emphasized that the IRS’s discretion to extend the period was not abused given the significant delay. The court also found that the retroactive revocation was justified under section 7805(b) because the initial application contained a misstatement of a material fact regarding the pension plan’s contribution formula, which affected the determination of the profit-sharing plan’s qualification. The court noted that the IRS’s function in issuing determination letters is based on the information provided, not on independent investigation.

Practical Implications

This decision underscores the importance of accuracy and timeliness in plan amendments and applications for IRS determination letters. Employers must ensure all material facts are correctly stated in applications and should not rely on the IRS to discover errors through independent investigation. The ruling also highlights the limited circumstances under which retroactive amendments are allowed, emphasizing the need for timely action within the remedial amendment period or to request an extension before its expiration. Practitioners should advise clients to monitor plan integration levels carefully, especially when multiple plans cover the same employees, to avoid disqualification due to excessive integration. This case has been cited in subsequent rulings to reinforce the IRS’s authority to revoke determinations retroactively when material facts are misstated.

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