Feichtinger v. Commissioner, 80 T. C. 239 (1983)

A defined benefit pension plan cannot be qualified if it allows for advance funding of anticipated cost-of-living adjustments before they become effective.

Summary

James N. Feichtinger, as administrator of a defined benefit pension plan, sought a declaratory judgment to challenge the IRS's adverse determination that the plan was not qualified under IRC section 401. The IRS's decision was based on the plan's provision allowing the actuary to anticipate future cost-of-living increases in calculating current contributions, which contravened section 1. 415-5(c)(1) of the Income Tax Regulations. The Tax Court upheld the IRS's determination, reasoning that the regulation prohibiting such advance funding was valid and consistent with congressional intent to prevent abuse of tax-favored treatment through premature deductions. This ruling underscores the importance of ensuring pension plans adhere strictly to regulatory guidelines regarding funding practices.

Facts

James N. Feichtinger, the plan administrator of the Consultants & Actuaries, Inc. Defined Benefit Pension Plan, filed for a declaratory judgment under IRC section 7476 to contest an adverse determination letter from the IRS. The IRS issued the letter on October 8, 1981, stating the plan was not qualified under IRC section 401 due to its provision in section 5. 1(f) of Article V. This provision allowed the actuary to consider future cost-of-living increases under IRC section 415(d)(1)(A) when determining funding contributions for the current year, which violated section 1. 415-5(c)(1) of the Income Tax Regulations.

Procedural History

The Consultants & Actuaries, Inc. Defined Benefit Pension Plan was adopted on March 16, 1979. A request for determination of its qualified status was filed with the IRS, and after several amendments, the IRS issued a final adverse determination letter on October 8, 1981. Feichtinger then filed a petition for declaratory judgment with the United States Tax Court, which upheld the IRS's determination on January 20, 1983.

Issue(s)

1. Whether a defined benefit pension plan's provision allowing the actuary to anticipate future cost-of-living increases under IRC section 415(d)(1)(A) for determining current year contributions violates section 1. 415-5(c)(1) of the Income Tax Regulations, thereby disqualifying the plan under IRC section 401?

Holding

1. Yes, because the plan's provision contravenes the regulation's prohibition on funding for anticipated cost-of-living adjustments before their effective date, which is a valid criterion for disqualifying the plan under IRC section 401.

Court's Reasoning

The Tax Court upheld the validity of section 1. 415-5(c)(1) of the Income Tax Regulations, which prohibits funding for anticipated cost-of-living adjustments before their effective date. The court reasoned that this regulation was consistent with the congressional intent to limit the tax-favored treatment associated with qualified pension plans, as expressed in the legislative history of IRC sections 401 and 415. The court emphasized that allowing advance funding would enable premature deductions and potentially lead to abuse of the tax system. Feichtinger's argument that such considerations should not affect the plan's initial qualification was rejected, as the court found the plan's language directly contravened the regulation. The court also noted that while the IRS's explanation of the determination may have evolved, the focus remained on the same objectionable provision of the plan.

Practical Implications

This decision clarifies that pension plans must adhere strictly to regulations regarding the timing of funding contributions. For attorneys and plan administrators, it is critical to ensure that plan language complies with regulations, particularly those prohibiting advance funding based on anticipated future adjustments. The ruling may influence how similar cases are analyzed, emphasizing the need for precise actuarial assumptions and funding methods that align with regulatory standards. Businesses and plan sponsors must review their plans to avoid disqualification and potential loss of tax benefits. Subsequent cases involving pension plan funding will likely reference this decision to uphold the principle of prohibiting advance funding of cost-of-living adjustments.

