O'Malley v. Commissioner, 96 T. C. 644 (1991)

A disqualified person is liable for excise tax under section 4975(a) for participating in a prohibited transaction by receiving plan benefits, even if they did not vote as a fiduciary to approve the transaction.

Summary

Thomas O'Malley, a trustee of the Teamsters' Pension Fund, was indicted for conspiring to bribe a U. S. Senator. The pension fund paid O'Malley's legal fees for his criminal defense, which he did not vote to approve but benefited from. The U. S. Tax Court held that O'Malley was subject to the excise tax under section 4975(a) of the Internal Revenue Code, as he was a disqualified person who participated in a prohibited transaction by receiving personal benefits from the pension fund. The court emphasized that participation in a prohibited transaction for tax purposes does not require active approval but can include merely receiving the benefits of the transaction.

Facts

Thomas O'Malley served as an employer trustee of the Central States, Southeast and Southwest Areas Pension Fund from 1978 to 1982. In 1981, O'Malley and others were indicted for conspiring to bribe a U. S. Senator. The pension fund's board of trustees, without O'Malley's vote, approved the payment of his legal defense costs. O'Malley's employer, C. W. Transport Co. , contributed to the pension fund but did not pay any part of his legal fees. The pension fund was later reimbursed for these payments by insurance companies. O'Malley was convicted of the charges and sentenced to prison.

Procedural History

The Commissioner of Internal Revenue determined deficiencies in excise tax against O'Malley for the years 1981-1984, asserting that the payment of his legal fees by the pension fund constituted a prohibited transaction under section 4975(a). O'Malley petitioned the U. S. Tax Court, which had previously ruled in a related case that the legal fees were personal to O'Malley and not taken in his fiduciary capacity. The Tax Court now considered whether O'Malley's receipt of these benefits subjected him to the excise tax.

Issue(s)

1. Whether Thomas O'Malley is subject to the excise tax imposed under section 4975(a) for receiving payments of his legal fees from the pension fund.

Holding

1. Yes, because O'Malley participated in a prohibited transaction by receiving

personal benefits from the pension fund, even though he did not vote as a fiduciary to approve the transaction.

Court's Reasoning

The court applied section 4975(a) of the Internal Revenue Code, which imposes an excise tax on disqualified persons who participate in prohibited transactions. O'Malley was a disqualified person under section 4975(e)(2)(A) and (H) due to his position as a fiduciary and officer of an employer whose employees were covered by the plan. The court clarified that participation under section 4975 includes receiving benefits from a transaction, not just approving it. The court cited previous cases and legislative history indicating that ERISA's standards are more stringent than traditional trust law, and that participation in a prohibited transaction for tax purposes does not require active approval. The court concluded that O'Malley's receipt of the legal fees constituted participation in a prohibited transaction, making him liable for the excise tax.

Practical Implications

This decision expands the definition of participation in prohibited transactions under ERISA, emphasizing that receiving benefits from a transaction can subject a disqualified person to excise tax, even if they did not approve the transaction. Legal practitioners advising fiduciaries of employee benefit plans must ensure that any payments from the plan to disqualified persons are carefully scrutinized to avoid triggering the excise tax. This ruling may deter fiduciaries from accepting personal benefits from the plans they manage, as they could be liable for taxes even if they abstain from voting on the matter. Subsequent cases have applied this broad interpretation of participation, reinforcing the need for strict adherence to ERISA's standards to protect plan assets.

