

PURPOSE

- (1) This transmits a complete reprint with changes for IRM 4.72.12, Employee Plans Technical Guidelines, Revocation of IRC 401(a) Plans and/or Trusts.

BACKGROUND

- (1) This IRM provides technical and administrative procedures in the event a qualified retirement plan (under IRC 401(a)) and/or trust (under IRC 501(a)) loses its tax exempt status.

NATURE OF MATERIAL

- (1) 4.72.12.2.2 (3), Effect on Employer, clarified.
- (2) Exhibit 4.72.12-1 Examples, revised to include a nonhighly compensated employee.
- (3) Editorial changes made throughout.

AUDIENCE

TE/GE (Employee Plans)

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4.72.12

Revocation of IRC 401(a) Plans and/or Trusts

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4.72.12.1
(12-31-2005)
Overview

- (1) Guidance is provided with regard to the technical and administrative procedures in the event a qualified retirement plan (under IRC 401(a)) and/or trust (under IRC 501(a)) loses its tax exempt status.

4.72.12.2
(12-31-2005)
Failure to Qualify in Operation

- (1) Some of the most common causes for a plan's failure to qualify in operation are:
- a. The plan has failed to meet the coverage requirements under IRC 410(b).
 - b. Contributions or benefits provided under the plan are discriminatory within the meaning of IRC 401(a)(4).
 - c. The plan and/or trust activity violates the exclusive benefit provision of IRC 401(a).
 - d. The plan has failed to follow the terms of the plan.
- (2) Generally, in pre-ERISA law, if a prohibited transaction occurred the trust lost its exemption; but IRC 4975 now substitutes excise tax and correction criteria in lieu of revocation. However, the payment of an excise tax does not prevent the EP specialist from proposing revocation if the exclusive benefit rule of IRC 401(a)(2) is violated.
- (3) D. O. No. 112, as revised, delegates to the Director, EP Examinations the authority to issue revocations of determination letters issued under the provisions of IRC 401, 403(a), 409 and 501(a) and this authority may be redelegated.
- (4) If a proposed revocation is based on a fiduciary violation of Part 4, Subtitle B of Title I of ERISA that resulted in an exclusive benefit rule violation under IRC 401(a) or, if the revocation involves collectively-bargained plans, such proposed revocation must be submitted for technical advice to the TE/GE Division Commissioner.

4.72.12.2.1
(12-31-2005)
Effective Date of Revocation

- (1) Except under circumstances described in (2) or (3) below, where a plan fails to qualify in operation for a year open for examination, the revocation should be effective beginning with the plan year in which the plan first failed to qualify. Such a revocation is not controlled by IRC 7805(b).
- (2) If the first year in which a plan failed to qualify could not be identified or is no longer open for examination, the revocation letter will merely state that any outstanding favorable determination letter previously issued on the date specified is revoked.
- (3) Except in rare or unusual circumstances, the revocation of a favorable determination letter is not applied retroactively with respect to the employer to whom the determination letter previously was issued or to an employer whose tax liability was directly involved in such determination if:
- a. There has been no misstatement or omission of material facts;
 - b. The facts subsequently developed are not materially different from facts on which the determination letter was based;
 - c. There has been no change in the applicable law;
 - d. The determination was originally issued with respect to a prospective or proposed transaction; and
 - e. The employer directly involved in the determination letter acted in good faith in reliance upon the determination letter and the retroactive revoca-

tion would be to his/her detriment. To illustrate, the tax liability of each employee covered by a determination letter relating to a pension plan of an employer is directly involved in such determination.

- (4) A qualified trust may lose its qualified status and then regain it. In this case the Service has maintained that after requalification all the assets of such trust are treated as assets of a qualified trust. See Rev. Rul. 72-368, 1972-2 C.B. 220, and Rev. Rul. 73-79, 1973-1 C.B. 194.
- (5) The tax treatment of distributions from a plan depends on the status of the plan at the time of distribution. Bartens v. Commissioner, 777 F.2d 1160 (6th Cir. 1985); Cass v. Commissioner, 774 F.2d 740; Woodson v. Commissioner, 651 F.2d 1094 (5th Cir. 1981).

4.72.12.2.2
(12-31-2005)
Effect on Employer

- (1) The employer can deduct the amount of the employer's contribution in the non-qualified year to the extent that the amount is includible in the gross income of employees participating in the plan only if separate accounts are maintained for each employee where there is more than one employee. See IRC 404(a)(5) and Reg. 1.404(a)-12 and also the examples in Exhibit 4.72.12-1.

Note: IRC 404(a)(6) does not apply to IRC 404(a)(5) deductions.

- (2) The regulations under IRC 402 and IRC 404, provide that if the status of the trust changes from nonexempt in one year to exempt in a succeeding year (third year), the deductibility by the employer (and inclusion in income by employees) of contributions made in the nonexempt year are not changed.
 - For example, a contribution to a plan in the second year for which it was not exempt would be deductible by the employer only to the extent such a contribution is deductible as a contribution to a nonexempt trust even though the trust regains qualified status in a later year (third year). However in such later year the entire trust would be treated as part of a qualified plan for purposes of determining the tax treatment of distributions even though the employer was, in such year, deducting part (or all) of a contribution made in the second year (during which the trust was not exempt) under deduction rules relating to nonqualified plans. Upon distribution of benefits from the trust the recipient has a basis equal to the part of the distribution previously includible in the recipient's income.
- (3) An employer has the burden to establish any claimed deduction for income tax purposes. Contributions that are not vested at the end of the plan year in which they are contributed to a nonqualified plan will be deductible in subsequent years as the contributions become vested. However, if a participant terminates prior to vesting in the nonexempt contribution and a forfeiture occurs the employer must be able to support the deduction claimed for such amount as includible in the gross income of employees as of or after reallocation.

4.72.12.2.3
(12-31-2005)
Effect on Employees

- (1) Prior to 8/2/69, the employee-participant was taxable to the extent of the non-forfeitable interest at the time the contribution was made.
- (2) After 8/1/69, the employee-participant is subject to tax when the employee's interest becomes substantially vested.

- a. The amount taxable to an employee-participant when a qualified plan becomes non-qualified is the amount contributed by the employer each year, while the plan is non-qualified, in which the employee is substantially vested.
 - b. So long as the plan remains nonqualified, amounts subsequently contributed by the employer to the trust (or premiums subsequently paid) are to be included in the income of the employee when contributed or paid to the trust (or insurer), or, if later, when the amounts including earnings thereon become substantially vested in subsequent years.
 - c. When a qualified plan becomes nonqualified, the employee-participant is not taxed on his/her account balance attributed to employer contributions while the plan was qualified or increases in the account balance attributed to trust earnings. For further explanation of taxability to an employee, see Reg. 1.402(b)-1(b).
- (3) For purposes of (2) above, the term “substantially vested” means that a participant’s interest is not subject to a substantial risk of forfeiture as defined in IRC 83(c)(1) and Regs. 1.83-3(b) and (c).
 - (4) The taxability examples in Exhibit 4.72.12-4 are based on Reg. 1.402(b)-1(b)(1) which provides that where a trust loses its exempt status, an employees’ gross income includes the value of the employee’s interest in the trust which is substantially vested and is attributable to employer contributions made for the employee while the trust was not exempt. Thus the only monies subject to taxation to the employee when a plan ceases to be qualified are those amounts allocated as employer contributions or forfeitures that are substantially vested or those amounts that become substantially vested after the trust loses its exempt status.
 - (5) Any loss in value of the assets purchased with employer contributions made during a taxable year ending with or within a taxable year of the trust for which it was not exempt is recognized to the participant only when all trust assets are distributed. See Rev. Rul. 71–251, 1971–1 C.B. 129. The employer would receive a deduction based on the full amount of the contribution included in the gross income of the participant.

4.72.12.2.4
(12-31-2005)
IRC 402(b)(4)

- (1) IRC 402(b) provides rules for taxation of beneficiaries of non-exempt employee benefit trusts. Under IRC 402(b), if a plan fails to satisfy the qualification requirements under IRC 401(a)—
 - a. the tax-exempt status of trust earnings is revoked;
 - b. employer deductions for contributions may be deferred or eliminated, and
 - c. all employees must include the value of post disqualification accruals or contributions in income in accordance with IRC 83. Thus, if contributions are made to the plan with respect to vested account or benefits, employees must include these amounts in income.
- (2) IRC 402(b)(4) contains special rules that apply if the plan fails to satisfy IRC 401(a)(26) and IRC 410(b). If the plan fails to satisfy either of these sections, each highly compensated employee (HCE) must include in income an amount equal to the employees’ entire vested accrued benefit not yet included in income. If, however, the plan is not qualified solely because it fails to satisfy the IRC 401(a)(26) or IRC 410(b) requirements, no adverse tax consequences are imposed on non-highly compensated employees. See also IRC 402(a)(4).

- a. Under the integrated approach to IRC 401(a)(4) and IRC 410(b) underlying the regulations, any failure to satisfy IRC 401(a)(4) is viewed by the preamble to the IRC 401(a)(4) regulations as failure to satisfy IRC 410(b).
- b. Consequently, failure to meet the requirements of IRC 401(a)(4) will cause IRC 402(b)(4) to apply with respect to a plan and will therefore subject HCEs to the special sanctions contained in that section.
- c. Similarly, if the plan satisfies all qualification requirements other than IRC 410(b) and IRC 401(a)(26), no adverse tax consequences will be imposed on NHCEs.

Example 1: Plan X was examined and determine to be nonqualified for two reasons: (i) the pension plan made distributions in single sums without obtaining spousal consent, and (ii) the plan covered only 8 of 60 employees. Of these 8 employees, 3 are HCEs.

Under IRC 402(b)(4)(A), all of Plan X's covered employees would incur adverse tax consequences. The 3 HCE's must include the present value of their entire nonforfeitable employer provided accrued benefits in income.

Example 2: Plan Y, a profit sharing plan, fails coverage under IRC 410(b). This is the only reason the plan is not qualified. The HCEs must include their entire employer provided account balances in income; and there are no adverse tax consequences to any other employee. The Plan Y trust is taxable. In the next year, the HCEs must include in income the value of their account at the end of the year less their "investment in the contract", i.e., the amount previously taxed.

4.72.12.3
(12-31-2005)

Revocation Procedures

- (1) When the investigation is concluded, discuss the issues with the employer and/or representative. (These procedures apply in the case of a trustee and non-trustee plan.)
 - a. Convert the trust to a taxable entity by securing Form 1041 for each year the plan and trust are not qualified. If the trustee(s) declines to file Form 1041, prepare a substitute for return.
 - b. Apply the discrepancy adjustment procedures for adjustments to Forms 1040 and 1120. For example, adjustments to the employer's deduction and the plan participant's income must be made to coincide with the requirements for deduction and taxation of amounts contributed under a nonqualified plan and trust. See IRM 4.71.4, Employee Plans Examination of Returns, Discrepancy Adjustments.
 - c. Follow appropriate procedures for contacting Examination function in cases where adjustments must be made to returns other than Forms 1040 and 1120.
 - d. Draft a revocation letter(s) and forward the case to Mandatory Review Staff.

4.72.12.3.1
(12-31-2005)

Examination Step

- (1) Consider all facts revealed in an examination before proposing revocation to an exempt trust because the adverse effect caused by such a revocation upon both the employer and the participants is significant. However, if facts and circumstances clearly show a plan has failed to qualify in operation, the revocation procedure should be initiated after the issue(s) is discussed fully with the group manager.

Exhibit 4.72.12-1 (12-31-2005)

Examples of Employer Deduction and Participant Taxation for Non-Qualified Plans

Example 1

This limitation is needed to distinguish from cases where 402(b)(4) applies. F is a nonhighly compensated employee of M Corporation whose profit-sharing plan has a calendar year plan year. F is a calendar year taxpayer. On 1/1/99, the plan ceased to be qualified. On that date F had an account balance of \$30,000 in which F had a nonforfeitable interest of 45% (\$13,500). On 12/1/99, the employer made a contribution to the plan of which \$7,000 was allocated to F's account. There were no forfeitures allocated to the account.

F had also completed an additional year of service for vesting and had a nonforfeitable right to 50% of such contribution (\$3,500).

For 1999, under Reg. 1.402(b)-1(b)(1), F would include in gross income \$3,500, the vested portion of the employer contribution made to the plan during the employer's taxable year during which the trust was not exempt. F does not include the value of the increase in his/her vested right to the account balance at 1/1/99 or the earnings thereon in income because these monies are attributable to employer contributions made to the plan while the trust was exempt. Assume no earnings are allocated in 1999 which are attributable to the \$7,000 contribution allocated on 12/1/99.

Under IRC 404(a)(5), M could deduct in 1999, \$3,500, the amount of the contribution includible in F's income.

Worksheet for Taxation of Participants in Nonqualified Defined Contribution Plans

Defined Contribution

Nonqualified year for which no earnings are allocated to nonqualified contributions and/or forfeitures.

A.	Employer contributions and forfeitures for participant for year:	\$7,000
B.	Multiply by participant's nonforfeitable percentage under the plan at the calendar year end:	x .50
C.	Amount includible in participant's income:	\$3,500

Example 2

S, a nonhighly compensated employee, first participated in the G Corp. money purchase pension plan on 1/1/95. The plan provides that forfeitures are used to reduce future employer contributions. These contributions are fixed by the plan at 5% of total compensation. S earns \$25,000 per year. Both S and the plan are on a calendar taxable year. The plan ceased to be a qualified plan on 1/1/99. On 12/15/99, a \$1,250 amount was credited to S's account. This amount consisted of \$1,100 of employer contributions and \$150 of forfeitures. S has a nonforfeitable right to 80% of this amount.

S would include in income for 1999 \$1,000 (\$1,250 x .80). The employer would deduct \$880, which is the portion of its contribution which was includible in S's income, (\$1100 x .80).

Exhibit 4.72.12-1 (Cont. 1) (12-31-2005)**Examples of Employer Deduction and Participant Taxation for Non-Qualified Plans**

Note: Although no part of the forfeiture allocated to S's account was deductible in this case, forfeitures includible in participants' income, would be deductible by the employer to the extent the employer could demonstrate that the forfeiture resulted from employer contributions made during a nonqualified year and not previously deducted. For example, if \$25 of the forfeitures in this case had resulted from such contributions, the employer would have been able to deduct an additional \$20, the amount includible by the employee, i.e., $(\$25 \times .8)$.

Worksheet for Taxation of Participants in Nonqualified Defined Contribution Plans

Defined Contribution

Nonqualified year for which no earnings are allocated to nonqualified contributions and/or forfeitures

A.	Employer contributions and forfeitures for participant for year*:	\$1,250
B.	Multiply by participant's nonforfeitable percentage under the plan at the calendar year end;	x .80
C.	Amount includible in participant's income:	\$1,000

* Contribution \$1,100; Forfeiture \$150

Example 3

F, a nonhighly compensated employee, is a participant in the S Corporation Profit-Sharing Plan. The plan calls for periodic contributions in an amount to be decided upon by the employer. This amount is to be allocated under a fixed formula to employees' accounts. The amount allocated is to be increased by forfeitures.

Both F and S Corp. are calendar year taxpayers. The plan ceases to be qualified on 1/1/97. On 12/15/97, \$7,250 is allocated to F's account.

This amount consists of a \$7,000 employer contribution and a \$250 forfeiture. F has a nonforfeitable right to 60% of his account balance for 1997.

F, under Regs. 1.402(b)-1(b)(1) and (2), would include in income for 1997, $\$7,250 \times .60$ or \$4,350. S Corporation would deduct \$4,200 the nonforfeitable part of the contribution, $\$7,000 \times .60$.

Worksheet for Taxation of Participants in Nonqualified Defined Contribution Plans

Nonqualified year for which no earnings are allocated to nonqualified contributions and/or forfeitures.

Exhibit 4.72.12-1 (Cont. 2) (12-31-2005)

Examples of Employer Deduction and Participant Taxation for Non-Qualified Plans

- A. Employer Contributions and forfeitures for participant for year*: \$7,250
 - B. Multiply by participant's nonforfeitable percentage under the plan at the end of the calendar year: x .60
 - C. Amount includible in participant's income: \$4,350
- *Contribution \$7,000; Forfeiture \$250

Example 4

P, a nonhighly compensated employee is a participant in the S Corp. profit sharing plan. The plan ceased to be a qualified plan on 1/1/98. P and the plan are calendar year taxpayers.

The following chart shows the history of P's account balance attributable to employer contributions made while the plan was qualified (pre-1998). Also shown are employer contributions and account balances attributable to employer contributions and earnings on these, during years for which the plan is not exempt..

Year Ending	Acct. Bal. + Earnings
9712	10,000
9812	12,000
9912	14,200
2000	15,845

Post 1997 Contributions

Year Ending	Employer Contribution	Nonforfeitable Right	Nonqualified Account Balance and Earnings
9812	1,000	70%	1,000
9912	1,000	80%	2,200
2000	1,000	90%	3,300

In 1998 P would include in income \$700, the nonforfeitable amount attributable to employer contributions made during a year when the plan was nonqualified. S would deduct \$700.

Exhibit 4.72.12-1 (Cont. 3) (12-31-2005)**Examples of Employer Deduction and Participant Taxation for Non-Qualified Plans**

In 1999, P would include in income the nonforfeitable portion of the 1999 employer contribution, \$800. Also, P would include the value of the nonqualified account (less the current year's allocation) multiplied by the increase in P's vesting (1,200 x .10) or \$120. Thus, P's total inclusion for 1999 is \$920.

In 2000, P would include in income \$900, the current year's employer contribution (\$1,000) multiplied by P's nonforfeitable portion (90%). Also, P would include the value of the nonqualified account (less the current year's contribution) \$2,300 multiplied by the increase in P's nonforfeitable percentage for the year (.1) or \$230. Thus, P's total inclusion for 2000 is \$1,130.

S Corporation's deductions are computed as follows:

1998:	\$700	nonforfeit. part of E'r contribution
1999:	\$800	nonforfeit. part of E'r contribution
	<u>\$100</u>	<u>increase in vesting in 1998 contrib.</u>
	\$900	Total deduction
2000:	\$900	nonforfeit. part of 2000 E'r contrib.
	100	increase in vesting in 1999 contrib.
	<u>100</u>	<u>increase in vesting in 1998 E'r contrib.</u>
	\$1,100	

1998 Worksheet for Taxation of Participants in Nonqualified Defined Contribution Plans**Defined Contribution**

Nonqualified year for which no earnings are allocated to nonqualified contributions and/or forfeitures

A.	Employer Contributions and forfeiture for participant for year*:	\$1,000
B.	Multiply by participant's nonforfeitable percentage under the plan at the calendar year end:	x .70
C.	Amount includible in participant's income:	\$700

*The taxable year of the participant during which the amounts were allocated if such amounts are employer contributions or forfeitures made during a taxable year of the trust for which it was not exempt.

1999

Nonqualified Years for which earnings are allocated to nonqualified contribution and/or forfeitures.

Exhibit 4.72.12-1 (Cont. 4) (12-31-2005)

Examples of Employer Deduction and Participant Taxation for Non-Qualified Plans

A.	Employer Contributions and forfeitures for participant for year:*	\$1,000
B.	Multiply by nonforfeitable percentage at the calendar year end:	x .80
C.	Subtotal:	\$800
D.	Total "nonqualified" account (other than current year allocation):	\$1,200
E.	Increase in vesting:	.10
F.	Amount includible in respect to increase in vesting (D x E):	\$120
G.	Total includible in gross income for second year (C + F):	\$920

* The taxable year of the participant during which the amounts were allocated if such amounts are employer contributions or forfeitures made during a taxable year of the trust for which it was not exempt.

2000

Nonqualified Years for which earnings are allocated to nonqualified contribution and/or forfeitures.

A.	Employer Contributions and forfeitures for participant for year:*	\$1,000
B.	Multiply by nonforfeitable percentage at the calendar year end:	x .90
C.	Subtotal:	\$900
D.	Total "nonqualified" account (other than current year allocation):	\$2,300
E.	Increase in vesting:	.10
F.	Amount includible in respect to increase in vesting (D x E):	\$230
G.	Total includible in gross income for second year (C + F):	\$1,130

* The taxable year of the participant during which the amounts were allocated if such amounts are employer contributions or forfeitures made during a taxable year of the trust for which it was not exempt.

Example 5

An employer maintains a qualified defined contribution plan. The employer's taxable year and the plan year both end on June 30. On 7/1/98, the plan loses its qualified status. On 6/30/99, the plan's allocation date, \$5,000 is contributed to the account of a calendar year, nonhighly compensated, employee who is 100% vested in his/her account balance. The tax consequences to the employee and the employer are as follows.

Exhibit 4.72.12-1 (Cont. 5) (12-31-2005)**Examples of Employer Deduction and Participant Taxation for Non-Qualified Plans**

Employee. Reg. 1.402(b)-1(a)(1) provides that a contribution made during a taxable year of the employer which ends with or within the taxable year of the trust for which it is not so exempt shall be included as compensation in the gross income of the employee for his/her taxable year during which the contribution is made, to the extent vested. Thus, the employee includes \$5,000 in gross income as compensation for the calendar year ending 12/31/99.

Employer. Reg. 1.404(a)-(12)(b)(1) provides that a deduction is allowable under IRC 404(a)(5) only in the taxable year of the employer in which or with which ends the taxable year of the employee in which an amount attributable to such contribution is includible in his/her income. Here, the employee has included the \$5,000 contribution in the year ending 12/31/99. This year ends within the employer's taxable year ending 6/30/2000. Thus, the employer will deduct the \$5,000 contribution for its taxable year ending 6/30/2000.

Example 6

F, a nonhighly compensated employee, is a participant in a noncontributory defined benefit pension plan that provides a benefit of 50% of the individual's high-5 average monthly compensation per month for life beginning at normal retirement age. The plan offers an automatic qualified 50% J & S which is fully subsidized. Normal retirement age is age 65, but an actuarially reduced benefit is available at age 55. F was hired at age 25 on 12/31/94. F is unmarried. On 12/31/99, F's high-5 average compensation was \$75,000. On 1/1/99, the plan ceased to be qualified. The plan uses the vesting schedule provided in IRC 416(b)(1).

In accordance with Reg. 1.402(b)-1 the amount of employer contributions deemed made during F's 1999 taxable year (assuming the plan and tax year are the calendar year) is determined as the excess of (a) the amount determined under the formula in Reg. 1.403(b)-1(d)(4) as of 12/31/99, over (b) the amount determined under that section as of 12/31/98.

To calculate the amount under (a) as of 12/31/99, multiply four quantities which are determined as follows under 1.403(b)-1:

- | | | |
|-----|--|-----------------|
| (1) | Projected annual pension @ normal retirement age assuming continued employment and current salary rate is:
\$75,000 x 50% = | <u>\$37,500</u> |
| (2) | The value of \$1 per year payable monthly for F's life beginning @ normal retirement age as defined in the plan. (The value is taken from Table I in Reg. 1.403(b)-1(d)(4)): | <u>10.63</u> |
| (3) | The level annual accumulation factor determined under Table II in Reg. 1.403(b)-(1)(d)(4) for 40 years of service (age 25 - 65): | <u>.0118</u> |
| (4) | The number of years of F's credited service at 12/31/99: | <u>5</u> |
| (5) | (1) x (2) x (3) x (4) = | <u>\$23,519</u> |

Exhibit 4.72.12-1 (Cont. 6) (12-31-2005)

Examples of Employer Deduction and Participant Taxation for Non-Qualified Plans

The amount under (b) is calculated in the same way but based on F's salary and service at 12/31/98:

(1)	Assuming F's high-5 compensation was \$62,500 @ 12/31/98, the projected benefit as of that date is: $\$62,500 \times 50\% =$	<u>\$31,250</u>
(2)	This value is unchanged since it depends only on normal retirement age:	<u>10.63</u>
(3)	This amount is also unchanged since it depends on total service (age 25 - 65):	<u>.0118</u>
(4)	The number of years of F's credited service at 1/1/98:	<u>4</u>
(5)	(1) x (2) x (3) x (4) =	<u>\$15,679</u>

The amount includible in F's income for the 1996 taxable year (c) is calculated as follows:

(1)	Amount under (a) above:	<u>\$23,519</u>
(2)	Amount under (b) above:	<u>\$15,679</u>
(3)	(1) - (2) =	<u>\$7,840</u>
(4)	F's non-forfeitable percentage for 1999:	<u>80%</u>
(5)	Amount includible (3) x (4):	<u>\$6,272</u>

If the plan is not requalified in 2000 the amount includible in F's income for 2000 is calculated in a manner similar to the calculations for 1999 except that the additional portion of the deemed contribution of \$7,840 which becomes vested in 2000 is also includible.

The amount determined under Reg. 1.403(b)-1 for F as of 12/31/2000, is determined as follows:

(1)	Assuming F's high-5 compensation at 12/31/2000 is \$82,000 his/her projected benefit is $\$82,000 \times 50\%$:	<u>\$41,000</u>
(2)	Value from Table I based on F's normal retirement age:	<u>10.63</u>
(3)	Level annual accumulation factor from Table II:	<u>.0118</u>
(4)	F's credited service @ 12/31/2000:	<u>6</u>
(5)	(1) x (2) x (3) x (4) =	<u>\$30,857</u>
(6)	The amount determined for F as of 12/31/99 (see above) =	<u>\$23,519</u>
(7)	(5) - (6) =	<u>\$7,338</u>
(8)	F's non-forfeitable percentage for 2000:	<u>100%</u>

Exhibit 4.72.12-1 (Cont. 7) (12-31-2005)**Examples of Employer Deduction and Participant Taxation for Non-Qualified Plans**

(9)	Increase in vested portion of contribution deemed made for 1999 (7840 x (1 - .8)):	<u>\$1,568</u>
(10)	Amount includible in F's income for 2000 (100% x 7338 + (9)):	<u>\$8,906</u>

If F chooses to use this method to determine the amount of employer contributions to be includible in his/her income for a specific taxable year the calculation is independent of amounts actually contributed to the plan by the employer.

For example, the full amount would be includible regardless of the fact the employer has received a waiver of the minimum funding standard for the plan year in question.

Reg. 1.403(b)-1 provides that a reasonable alternative method based on recognized actuarial principles and consistent with the provisions of the plan and the funding method adopted by the plan sponsor may be used. Such a method would provide deemed contributions which are consistent with required contribution patterns (disregarding any funding waivers) even if the plan is fully funded and no actual employer contributions are required or made.

These amounts are deductible, if at all, under IRC 404(a)(5). That section requires separate accounts as a pre-condition for a deduction. Consequently, if there is more than one participant under a nonqualified defined benefit plan except fully insured individual contracts, no deduction is available to the employer, even though amounts are includible in the participants' income.,

Example 7

R, a nonhighly compensated employee, is a participant in a defined contribution plan which ceased to be qualified on 1/1/99. In December 1999, a \$1,000 employer contribution is allocated to R's account. This amount is used to purchase 50 shares of common stock at \$20 per share. R has a nonforfeitable right to 100% of R's account.

In 2000, a further \$1,000 is allocated to R's account. The stock purchased in 1999 is now selling for \$15 per share on a national exchange and R's 50 shares have a fair market value of \$750. For 2000 R would include \$1,000 in income.

If R's nonforfeitable interest was less than 100% in 1999, she would include in income an amount which is the result of the increase in her nonforfeitable interest multiplied by the current (2000) value of the account. Her basis would increase accordingly.

Thus if R's nonforfeitable percentage increased from 60% on 12/31/99 to 70% on 12/31/2000, R would include in income \$75. This is the result of multiplying the increase in R's nonforfeitable interest (10%) by the value of the account on 12/31/2000 minus the 2000 contribution (\$750).

1999 Calculation: \$1,000 @ 60% =	\$600.00
(1999 Contribution)	
2000 Calculation: \$1,000 @ 70% =	\$700.00
(2000 Contribution)	

Exhibit 4.72.12-1 (Cont. 8) (12-31-2005)

Examples of Employer Deduction and Participant Taxation for Non-Qualified Plans

<u>1999 Acct. Balance</u>	<u>2000 Contribution</u>	<u>Acct. Balance</u>	<u>Change in Vesting</u>	<u>Taxable Amt.</u>
\$1,750.00	-\$1,000.00	= 750.00	x. 10	= \$75.00

Any losses in the value of R's account would not be recognized by R until distribution of R's entire interest. See Rev. Rul. 71-252--1971-1 C.B. 129.

1999

**Worksheet for Taxation of Participants in
Nonqualified Defined Contribution Plan**

Defined Contribution

Nonqualified year for which no earnings are allocated to nonqualified contributions and/or forfeitures

A.	Employer Contributions and forfeitures for participant for year*:	\$1,000
B.	Multiply by participant's nonforfeitable percentage under the plan at the calendar year end:	x .60
C.	Amount includible in participant's income:	\$ 600

2000

Nonqualified Years for which earnings are allocated to nonqualified contribution and/or forfeitures.

A.	Employer Contributions and forfeitures for participant for year*:	\$1,000
B.	Multiply by nonforfeitable percentage at the calendar year end:	x .70
C.	Subtotal:	\$ 700
D.	Total "nonqualified" account (other than current year allocation):	\$ 750
E.	Increase in vesting:	.10
F.	Amount includible in respect to increase in vesting (D x E):	\$ 75
G.	Total includible in gross income for second year (C + F):	\$ 775

Exhibit 4.72.12-1 (Cont. 9) (12-31-2005)

Examples of Employer Deduction and Participant Taxation for Non-Qualified Plans

* The taxable year of the participant during which the amounts were allocated if such amounts are employer contributions or forfeitures made during a taxable year of the trust for which it was not exempt. Upon distribution of benefits from the trust the recipient has a basis equal to the part of the distribution previously includible in the recipient's income.