Internal Revenue Service

Department of the Treasury
Washington, DC 20224

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CC:INTL:1 – PLR-152486-03
Date:
October 31, 2003

In Re:

TY:

Legend

US Corp	=
Year 1	=
Plan	=
X	=
Y	=
Z	=
Plan Administrator	=
Trustee	=
Date B	=
Date C	=

Dear :

This is in response to a letter dated August 27, 2003, requesting a ruling under the United States-Federal Republic of Germany income tax convention, signed on August 29, 1989 ("Treaty"), with respect to distributions from the Plan to certain nonresident alien participants who reside in Germany.

The ruling contained in this letter is based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

FACTS

US Corp established the Plan in Year 1. US Corp represents that the Plan is a non-contributory stock bonus plan for foreign employees of US Corp and its foreign subsidiaries. The trust forming part of the Plan is a qualified trust under section 401(a) of the Internal Revenue Code. Approximately X participants currently have accounts under the Plan, including approximately Y active and Z terminated participants who are residents of Germany. The remaining participants include active and terminated participants who reside in other foreign countries. Most of these participants performed all of their services for US Corp and its foreign subsidiaries abroad, although a small percentage also performed services in the United States and received contributions under the Plan for these services. This ruling request pertains only to those active or terminated participants who are residents of Germany, who are not citizens of the United States, and who either performed no services for US Corp and its subsidiaries in the United States or performed services only for very short periods in the United States (i.e., no more than 183 days in the aggregate in any calendar year) (referred to herein as the "German Participants").

US Corp and its foreign subsidiaries made profit-sharing contributions to the Plan with respect to their employees who participated in the Plan from its inception until such time as contributions were discontinued. US Corp has represented that in the case of the German Participants, all contributions were made by a foreign subsidiary of US Corp, and that such contributions were not reimbursed by US Corp or by any U.S. affiliate.

Except to the extent required to meet the cash requirements of the trust under the Plan, all employer contributions to the Plan were invested in common stock of US Corp, and dividends issued on US Corp common stock held by the Plan were reinvested in common stock of US Corp. The Plan maintained accounts for each participant, which represented the participant's interest in Plan contributions and earnings.

Under the Plan, a participant could make certain limited withdrawals from the Plan and, in any event, the participant or the participant's beneficiary was entitled to receive the full amount credited to his or her account upon the participant's retirement, disability, death, or termination of employment with five years of service. In the event the value of a terminated participant's account exceeded a specified dollar amount, the participant could elect to defer payment of the account until a later date. Distributions under the Plan to terminated participants were payable in stock of US Corp or cash, at the election of the participant.

The Plan is administered in the United States by the Plan Administrator, whose members are appointed by US Corp's Board of Directors, or by delegates of the Plan Administrator. The assets of the Plan are held in a United States trust by the Trustee.

US Corp terminated the Plan effective Date B, at which time US Corp applied to the Internal Revenue Service for a determination that the termination would not affect the Plan's tax-qualified status. A favorable determination letter was issued with respect to the termination on Date C.

In connection with the termination of the Plan, all Plan accounts will be paid to all participants, both active and terminated participants, in lump-sum distributions. Plan participants will be entitled to elect to receive their distributions in the form of either US Corp common stock or cash. It is anticipated that most of the German Participants will receive their distribution in the form of US Corp common stock. German Participants who have already retired or terminated employment after satisfying the Plan's vesting requirements are entitled to receive a distribution of the full amount credited to their Plan accounts independent of the Plan termination.

RULING REQUESTED

Distributions to German Participants in connection with the termination of the Plan will be exempt from U.S. income tax under the Treaty.

LAW AND ANALYSIS

Section 871(a) of the Code provides, generally, that a nonresident alien individual is subject to a 30-percent tax on amounts received as interest (other than original issue discount as defined in section 1273), dividends, rents, salaries, wages, premiums, annuities, compensations, remunerations, emoluments, and other fixed or determinable annual or periodical gains, profits, and income to the extent the amount so received is from sources within the United States, but only to the extent the amount so received is not effectively connected with the conduct of a trade or business within the United States.

Section 871(b) of the Code and section 1.871-8(b)(2) of the Income Tax Regulations provide, in part, that a nonresident alien individual engaged in a trade or business within the United States during the taxable year is taxed as provided in section 1 of the Code on taxable income which is effectively connected with the conduct of a trade or business within the United States. Section 1.864-2(a) of the Income Tax Regulations provides that the term "engaged in trade or business within the United States" generally includes the performance of personal services within the United States at any time within the taxable year. Section 864(c)(6) of the Code provides, in general, that payments of deferred compensation to a nonresident alien individual that are attributable to services performed in another year will be treated as income effectively connected with the conduct of a U.S. trade or business in the year of receipt if they would have been so treated if the income were taken into account in the year the services were performed.

Section 861(a)(3) of the Code provides that compensation for labor or personal services performed in the United States will be treated as income from sources within the United States. Section 862(a)(3) of the Code provides that compensation for labor or personal services performed outside the United States will be treated as income from sources outside the United States.

Employer contributions to an annuity or pension plan represent compensation for personal services. See Rev. Rul. 56-82, 1956-1 C.B. 59. For purposes of determining the source of pension distributions from a U.S. pension plan, amounts attributable to employer contributions with respect to services performed within the United States are income from sources within the United States, amounts attributable to employer contributions with respect to services performed outside the United States are income from sources outside the United States, and amounts attributable to earnings and accretions with respect to employer contributions are income from sources within the United States. Rev. Rul. 79-388, 1979-2 C.B. 270.

Section 894(a) of the Code provides that the provisions of the Internal Revenue Code will be applied with due regard to any treaty obligation of the United States that applies to the taxpayer.

Paragraph 1 of Article 18 (Pensions, Annuities, Alimony, and Child Support) of the Treaty provides that “pensions and other similar remuneration derived and beneficially owned by a resident of a Contracting State in consideration of past employment” are taxable only in that Contracting State. The term "pension" is not defined in the Treaty. The Technical Explanation prepared by the Treasury Department states that the rule of paragraph 1 applies to both periodic and lump-sum payments.

Paragraph 1 of Article 15 (Dependent Personal Services) of the Treaty provides that “salaries, wages, and other similar remuneration” derived by a resident of a Contracting State are taxable only in that Contracting State, unless the employment is exercised in the other Contracting State. Paragraph 2 provides that to the extent remuneration is derived from an employment exercised in the other Contracting State, such remuneration may also be taxed by the other Contracting State. However, the other Contracting State may not tax the remuneration if: (1) the recipient of such remuneration is present in the other Contracting State for a period or periods not exceeding in the aggregate 183 days in the calendar year concerned; (2) the remuneration is paid by, or on behalf of, an employer who is not a resident of the other Contracting State; and (3) the remuneration is not borne by a permanent establishment or a fixed base that the employer has in the other Contracting State. Article 15 is subject to the provisions of Article 18, to the extent those provisions apply.

Article 21 (Other Income) of the Treaty provides that items of income of a resident of a Contracting State, wherever arising, not dealt with elsewhere in the Treaty, are taxable only in the State of residence.

Clayton v. United States, 33 Fed. Cl. 628 (1995), aff'd without published opinion, 91 F. 3d 170 (Fed. Cir.), cert. denied, 519 U.S. 1040 (1996), addressed the application of the United States-Canada income tax convention ("Canadian Treaty") to cash distributions to nonresident aliens who were residents of Canada from a U.S. trust forming part of an employee stock ownership plan. The trust was a qualified trust under section 401(a). The Federal Circuit held that the earnings and accretions portion of the distributions did not constitute "salaries, wages and other similar remuneration" for purposes of Article XV (Dependent Personal Services) of the Canadian Treaty. Because such income was not covered elsewhere in the Canadian Treaty, the Federal Circuit held that it was covered by Article XXII (Other Income).

Based solely on the information submitted and the representations made by the taxpayer, we conclude that distributions by the Plan to German Participants in connection with the termination of the Plan will be entirely exempt from U.S. income tax under the Treaty.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter. No opinion is expressed as to whether distributions to participants other than German Participants will be subject to U.S. income tax. No opinion is expressed as to whether a German Participant is or will be a resident of Germany for purposes of the Treaty. See section 4.01(14) of Rev. Proc. 2003-7, 2003-1 I.R.B. 233, 234.

This ruling is directed only to the taxpayer(s) requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

In accordance with the Power of Attorney on file with this office, and section 8.02(2) of Rev. Proc. 2003-1, 2003-1 I.R.B. 1, 25, copies of this letter are being sent to your authorized representatives.

Sincerely,

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M. Grace Fleeman
Senior Counsel, Branch 1
Office of Associate Chief Counsel
(International)