UNITED STATES COURT OF APPEALS
for the Fifth Circuit

No. 92-5226
Summary Calendar

CURTIS G. GRUMBLES and LINDA S. GRUMBLES,

Petitioner-Appellant

VERSUS

COMMISSIONER OF INTERNAL REVENUE,

Respondent-Appellee

Appeal from a Decision of the United States Tax Court
7809 90

June 30, 1993

Before JOLLY, DUHÉ, AND BARKSDALE, Circuit Judges.

PER CURIAM:[1]

Appellants, Curtis G. Grumbles and Linda S. Grumbles[2] appeal the decision of the United States Tax Court that they did not make a valid election under Section 1124 of the Tax Reform Act of 1986[3] ("TRA") to treat the qualified retirement plan distribution received in 1987 as if it were received in 1986. We reverse.

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[1] Local Rule 47.5 provides: "The publication of opinions that have no precedential value and merely decide particular cases on the basis of well-settled principles of law imposes needless expense on the public and burdens on the legal profession." Pursuant to that Rule, the Court has determined that this opinion should not be published.

[2] References to "taxpayer" are to Curtis G. Grumbles. His wife, Linda S. Grumbles, is a party because she filed a joint return with Curtis for the year in issue.

[3] Pub. L. 99-514, 100 Stat. 2065.

Background

Curtis G. Grumbles began employment with Brown & Root U.S.A., Inc. in 1976 and began participating in a qualified retirement plan to which both Grumbles and Brown & Root contributed beginning one year later.[4]

On December 18, 1986, Grumbles left Brown & Root to work elsewhere. Consequently, he requested full payment of the tax-deferred funds in his pension plan account. On February 23, 1987, Grumbles received a lump sum distribution of $36,162.42, the total in the account. The distribution was comprised entirely of contributions by Brown & Root and was fully taxable. Grumbles had previously withdrawn from the plan all of his contributions.

When Grumbles received the lump-sum distribution, Brown & Root provided him with a summary of the federal regulations concerning the taxable portion of the distribution. Grumbles was aware that he could "roll over" the distribution into another qualified retirement plan and thereby continue to defer taxation. He did not do so, however, because he did not want to tie up the money. The taxpayer timely filed a tax return for 1986, but did not include the distribution in that return.

In general, amounts distributed from a qualified pension or profit-sharing plan are taxable to the recipient in the year of

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[4] In general, a qualified retirement plan is a deferred compensation arrangement in which the employee is not taxed when the benefits are earned but only when they are received. I.R.C. § 401.

distribution. I.R.C. § 402(a)(1).[5] For distributions received before January 1, 1987, the Code provided that a taxpayer who received a lump sum distribution from a qualified plan could compute tax due on that amount by the "10-year averaging" method. I.R.C. § 402(e)(1). The averaging method was desirable because it allowed taxpayers to determine the tax due on the distribution as if it were received in ten equal annual installments. Tax was then calculated on one-tenth of the amount of the distribution and multiplied by ten. I.R.C. § 402(e)(1)(B), (C). Ultimately, the effect of the averaging method lowered the tax due on the distribution.

Under the Tax Reform Act of 1986, 5-year averaging replaced the 10-year averaging method for distributions received after December 31, 1986. TRA § 1122(a)(2), 100 Stat. 2466. Additionally, 5-year averaging was restricted to taxpayers who had reached age 59-1/2 at the time of the distribution.[6] TRA § 1122(a)(1), 100 Stat. 2466. The Act also added Section 72(t) to the Code, which imposed a 10-percent penalty on early withdrawals from any qualified retirement plan.

Congress did provide an exception to the elimination of the 10-year averaging method for a small group of taxpayers. TRA § 1124, 100 Stat. 2475. Section 1124(a) of the Tax Reform Act of 1986 provides that

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[5] Unless otherwise indicated, all statutory references are to the Internal Revenue Code in effect for the taxable year in issue.

[6] Grumbles was only age 35 at the time of the distribution.

> (a) IN GENERAL. -If an employee separates from service during 1986 and receives a lump-sum distribution (within the meaning of section 402(e)(4)(A) of such Code) after December 31, 1986, and before March 16, 1987, on account of such separation from service, then, for purposes of the Internal Revenue Code of 1986, such employee may elect to treat such lump-sum distribution as if it were received when such employee separated from service.

This provision enabled a taxpayer who qualified for its benefits to elect to treat a lump-sum distribution actually received in 1987 as having been received in 1986. This allowed a taxpayer to take advantage of the 10-year averaging and avoid the 10 percent early withdrawal penalty under I.R.C. § 72(t). It is undisputed that Grumbles falls under this exception.

Section 1124(a) does not provide the time or manner in which the election is to be made. The 1987 version of Form 4972 and Notice 87-13, 1987-1 C.B. 443, however, state that the election under 1124(a) must be made on a 1986 return (or amended 1986 return) filed by the due date for the 1987 tax return. In addition, a statement that the distribution is to be treated as a Section 1124 lump-sum distribution must be attached.

At the close of the 1987 tax year, petitioners took their return information to National Business Consultants ("NBC") for preparation of their 1987 tax return. The return information included the Form 1099R, which reflected the February 1987 lump-sum distribution, and it also included the information on the tax treatment of distributions received from Brown & Root.

During the first consultation with Charlotte Faulkner of NBC, Grumbles discussed the possibility that he might have to amend his 1986 return to obtain optimal tax treatment of the lump-sum distribution. When he later picked up his completed return, he relied on Faulkner who determined that he did not have to amend the 1986 return to obtain income averaging. His lump-sum distribution was reported and taxed under 5-year averaging on the originally filed 1987 return. This was in error.[7] Grumbles was not eligible for either 5-year or 10-year income averaging in 1987. Grumbles signed and timely filed this return.

The Internal Revenue Service notified Grumbles that he was not eligible for 5-year averaging and calculated the tax due on the lump-sum distribution using ordinary income tax rates. Grumbles filed amended income tax returns for 1986 and 1987 on December 15, 1989. I.R.C. section 6501(a) provides 3 years for filing an amended return. Both of the amended returns were timely filed.

On the amended 1987 return, Grumbles eliminated the tax attributable to the 5-year averaging of the lump-sum distribution as originally reported. This return reflected a refund due of $4,049. On the amended 1986 return, Grumbles reported his lump-sum distribution and calculated the tax under 10-year averaging. This return reflected additional tax due of $3,542. Grumbles requested that the refund from 1987 be offset against the tax due in 1986, and did not remit any payment to the IRS.

On January 24, 1990, the taxpayer received a statutory notice of deficiency from the Commissioner which redetermined the income tax due for 1987. Tax was calculated on the distribution without

[7] Grumbles was not entitled to elect this method because he was not age 59 1/2 at the time of the distribution.

the benefit of any averaging method. In addition, the Commissioner determined that Section 72(t) mandated the imposition of a 10 percent early withdrawal penalty on the amount of the distribution included in income for 1987.[8]

Grumbles filed a petition in the United States Tax Court for a redetermination of the deficiency. After receiving a stipulation of facts and legal briefs, the Tax Court decided in favor of the Commissioner.

Discussion

Grumbles argues that even though he did not follow the exact instructions for electing the 10-year averaging method for his lump-sum distribution, he should be entitled to relief under § 1124(a). We agree.

This Court reviews Tax Court decisions under the same standard used for civil actions decided by a federal district court. See I.R.C. § 7482(a). All facts were stipulated. The Tax Court's conclusions of law are reviewed de novo. Dresser Industries, Inc. v. Commissioner, 911 F.2d 1128, 1132 (5th Cir. 1990).

The Tax Reform Act of 1986 made sweeping changes in the taxation of lump-sum distributions. Prior to the Act, a taxpayer receiving a lump-sum distribution was generally entitled to minimize the income tax on the distribution by electing 10-year averaging and was not subject to the 10% early withdrawal penalty under I.R.C. § 72(t). In drafting the Act, Congress recognized that those taxpayers who separated from service in late 1986 but

[8] Total tax due, according to the notice, was $10,213.

did not receive their distributions until 1987 would get the worst of both alternatives. First, a cash basis taxpayer would have to report the lump-sum distribution in 1987, the year received and the Act greatly restricted the use of income averaging beginning in that year. Secondly, if the taxpayer did not qualify for the limited availability of income averaging, he would also be subject to the 10% early withdrawal penalty. As a result, Congress enacted § 1124(a) to provide relief for this limited group of taxpayers. The Grumbles fall squarely in this group Congress intended to help with the § 1124(a) transition rule.

The Grumbles elected §1124(a) relief on a timely filed amended 1986 return. This return was not, however, filed by the due date of their 1987 return as required by the instructions on Form 4972 or Notice 87-13. On his 1987 return, Grumbles erroneously used 5-year averaging for the distribution. This error was corrected on an amended 1987 return. By using the 5-year averaging method, albeit erroneously, Grumbles obviously intended to take advantage of the relief provisions. And as succinctly stated by the Tax Court in Younger v. Commissioner, 64 T.C.M. (CCH) 90 (1992), "the fact remains that the structure of Form 4972 is at best confusing."

Section 7805 gives the Secretary authority to issue regulations including specifying the time and manner for making elections. Merritt v. Commissioner, 64 T.C.M. (CCH) 397 (1992). The Secretary has promulgated no regulations under TRA § 1124(a). Id. The Tax Court also stated in Younger v. Commissioner

> The statutory provision is silent as to the manner of reporting except to the extent that the phrase "for the

> purposes of the Internal Revenue Code of 1986" could be said to encompass the time for reporting. Nor does the legislative history cast any light on the issue. The only reference to the transitional provision conceivably applicable to the issue involved herein is contained in the report of the staff of the Joint Committee on Taxation which uses a similar phrase, i.e., "for Federal tax purposes".[9]

In both Younger and Merritt, the Tax Court disregarded the instructions to Form 4972 and Notice 87-13. The court interpreted § 1124(a) liberally in order to comply with the intent of Congress in fashioning this relief provision. "We think it important to emphasize that we are dealing with a transitional provision of limited applicability and with a relief provision which should be liberally construed." Id. We conclude that the Commissioner suffers no prejudice by allowing the election to be made on a timely filed amended 1986 return filed after the due date for the 1987 return (including extensions) and that the petitioners in this case are entitled to the relief that § 1124(a) sought to give.

For the foregoing reasons, the judgment of the Tax Court is reversed, and judgment is rendered in favor of Grumbles for a refund of $507.00.

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[9] 64 T.C. M. (CCH) 90, 92 (1992).