

Announcement and Request for Comments on Certain Plans of State and Local Government Employers under Section 457.

Announcement 2000-1

Purpose

The Internal Revenue Service (IRS) is considering the proper treatment of amounts under certain plans of state and local governments. This announcement provides interim information about the reporting requirements that apply to these plans. The information contained in this announcement will apply until further guidance is issued by the Service.

Background

Section 457 plans are nonqualified deferred compensation plans established by state and local government and tax-exempt employers. Under section 457(e)(11) of the Internal Revenue Code, certain bona fide sick, vacation, compensatory time, severance pay, disability pay or death benefit plans are treated as not providing for the deferral of compensation and are therefore excluded from section 457.

If a plan is not a bona fide plan described in section 457(e)(11), the proper reporting of amounts under the plan generally depends on whether the plan is an eligible plan that meets the requirements of section 457(b) or an ineligible section 457(f) plan that does not meet these requirements. In order to be an eligible plan under section 457(b), the plan must meet a number of requirements, including the requirement that the amounts deferred for each year must generally not exceed the lesser of \$8000 (for 1999) or 33 1/3 percent of compensation and must be subject to restrictions on the time of distribution.

Under section 457(a), compensation deferred under an eligible plan, and the income attributable to that deferred compensation, is not includible in gross income until the taxable year in which the amounts are actually paid or made available to the plan participant or other beneficiary. Similarly, if a plan is a bona fide severance pay plan described in section 457(e)(11), amounts under the plan are generally not includible in gross income until paid or made available. In contrast, amounts under a plan described in section 457(f) are included in the participant or beneficiary's gross income for the first taxable year in which there is no substantial risk of forfeiture of the rights to the compensation.

Timing of reporting of payments under certain plans

Under this interim guidance by the Service, state and local governments should not report amounts, on either a Form 1099 or a Form W-2, for any year prior to the year in which the participant or beneficiary is in actual or constructive receipt of these amounts, if the amounts are provided under the following type of plan:

- The plan was in existence on December 22, 1999.
- The plan is a broad-based plan maintained by a state or local government employer primarily for non-highly compensated employees.
- The plan is nonelective. That is, the plan must not provide the participant with a choice between current and future compensation.
- The plan has been treated by the state or local government as a bona fide severance pay plan under section 457(e)(11) for those years before calendar year 1999 in which the plan was in existence.
- The plan satisfies the following three requirements:
 - a. Payments under the plan are designed to provide supplemental income for a transitional period, rather than to provide retirement income.
 - b. Payments under the plan are made only after separation from service with the employer, including retirement.
 - c. Payments are completed within a short period of time, not to exceed 5 years, after separation from service.

Solely for purposes of this announcement, a plan that provides severance pay benefits as described in §31.3121(v)(2)-1(b)(4)(iv)(B) of the Regulations will be treated as satisfying (a), (b) and (c) above.

REQUEST FOR PUBLIC COMMENT

The Service and the Treasury Department understand that, in the absence of formal guidance, many state and local governments maintain plans with the above characteristics under the belief that these plans are “bona fide severance pay plans” within the meaning of section 457(e)(11), and accordingly would not be subject to the income inclusion provisions applicable to ineligible section 457(f) plans. The Service

and the Treasury Department are now considering guidance under section 457 with respect to certain plans of state and local government and tax-exempt employers and are requesting comments on what types of plans maintained by state and local government and tax exempt employers are properly considered bona fide severance pay plans for purposes of section 457. Send written comments to: Internal Revenue Service, Attn: CC:DOM:CORP:R (Section 457 Plans), Room 5201, P.O. Box 7604, Ben Franklin Station, Washington, D.C. 20044. Written comments may be hand delivered Monday through Friday between the hours of 8 a.m. and 5 p.m. to: Internal Revenue Service, Courier's Desk, Attn: CC:DOM:CORP:R (Section 457 Plans), 1111 Constitution Avenue, N.W., Washington, D.C. 20224. Alternatively, written comments may be submitted electronically via the Internet by selecting the "Tax Regs" option on the IRS Home Page, or by submitting them directly to the IRS Internet site at: http://www.irs.gov/tax_regs/regslst.html.

Comments should be received by February 20, 2000.

FOR FURTHER INFORMATION CONTACT: Cheryl Press of the Office of Associate Chief Counsel (Employee Benefits and Exempt Organizations) at (202) 622-4606 (not a toll-free number).