Part III. – Administrative, Procedural and Miscellaneous

Transition Relief for Indian Tribal Governmental Plans

Notice 2006-89

I. Purpose

This notice summarizes the changes made to § 414(d) of the Internal Revenue Code (the Code) by section 906 of the Pension Protection Act of 2006 (PPA ‘06) under which plans established and maintained by Indian tribal governments and certain related entities are governmental plans. This notice also provides transition relief under a reasonable and good faith standard with respect to compliance with the PPA ’06 changes to § 414(d) pending further guidance, and invites comments from the public on whether additional transition issues need to be addressed. In addition, this notice provides approaches that give Indian tribal governments until September 30, 2007, to implement a new plan for commercial employees to satisfy the reasonable and good faith compliance standard as part of this transitional relief.

II. Background

Section 414(d) of the Code generally provides that a “governmental plan” includes a plan established and maintained for its employees by the Government of the United States, by the government of any State or political subdivision thereof, or by any agency or instrumentality of any of the foregoing. A governmental plan is exempt from many of the plan qualification requirements under § 401(a) and other sections of the Code. For example, governmental plans are exempt from the minimum participation and vesting requirements under §§ 410 and 411, certain nondiscrimination and coverage requirements, funding requirements under § 412, and the joint and survivor annuity rules under § 417. See the last sentence of § 401(a) (the flush language following §401(a)(36)).

PPA ’06 changed § 414(d)\footnote{Section 906(a) of PPA ’06 made similar amendments to section 3(32) and section 4021(b)(2) of the Employee Retirement Income Security Act of 1974 (ERISA).} to amend the definition of “governmental plan” with respect to plans of an Indian tribal government, a subdivision of an Indian tribal government, or an agency or instrumentality thereof (ITG). Section 906(a)(1) of PPA ’06 states:

The term ‘governmental plan’ includes a plan which is established and maintained by an Indian tribal government (as defined in section 7701(a)(40)), a subdivision of an Indian tribal government (determined in accordance with section 7871(d)), or an agency or instrumentality of either, and all of the participants of which are employees of such entity substantially all of whose services as such an employee are in the performance of essential governmental functions but not in the
performance of commercial activities (whether or not an essential government function).

The Joint Committee on Taxation’s Technical Explanation\(^2\) provides that an employee all of whose services for an ITG are in the performance of essential governmental services and not in the performance of commercial activities (whether or not such activities are an essential governmental function) is an employee who can be covered under a governmental plan as described in § 414(d). For example, a governmental plan includes a plan of a tribal government all of the participants of which are teachers in tribal schools, but a governmental plan does not include a plan covering tribal employees who are employed by a hotel, casino, service station, convenience store, or marina operated by a tribal government.

Section 906(c) of PPA ’06 provides that the amendments made by section 906 apply to any year beginning on or after the date of enactment, which is August 17, 2006. The Joint Committee on Taxation’s Technical Explanation (p. 244) states that the amendments apply to plan years beginning on or after the date of enactment.

Under section 1107 of PPA ’06, a plan amendment made pursuant to any amendment made by PPA ’06 may be retroactively effective, and does not violate the anti-cutback rules of § 411(d)(6) of the Code, except as provided by the Secretary of the Treasury, if, in addition to meeting the other applicable requirements, the amendment is made on or before the last day of the first plan year beginning on or after January 1, 2009 (2011 in the case of a governmental plan). Thus, an ITG must operate in accordance with the applicable changes to § 414(d) made by PPA ’06 as of the related PPA ’06 effective date, i.e., the first day of the first plan year beginning on or after August 17, 2006. Further, a plan established and maintained by an ITG that is designed to be a governmental plan under § 414(d) as amended by PPA ’06 must be amended to the extent necessary to reflect these changes by the last day of the first plan year beginning on or after January 1, 2011. This relief applies only if the amendment is effective as of the related PPA ’06 effective date and the plan has been operated in accordance with the amendment.

III. Transition Relief

A. Reasonable Good Faith Compliance Pending Guidance

1. In General. The IRS and the Department of the Treasury anticipate issuing guidance on § 414(d) of the Code, including the amendment made by section 906 of PPA ’06. Until such guidance is issued, a plan established and maintained by an ITG for its employees (ITG plan) will be treated as satisfying the requirements of section 906(a)(1) of PPA ’06 to be a governmental plan under § 414(d) of the Code if it complies with

\(^2\) Joint Committee on Taxation, Technical Explanation of H.R. 4, the “Pension Protection Act of 2006” as passed by the House on July 28, 2006, and considered by the Senate on August 3, 2006 (JCX-38-06), August 3, 2006, 109th Cong., 2nd Sess. 244 (2006)
those requirements based on a reasonable and good faith interpretation of the amendment made by section 906(a)(1) of PPA ‘06.

2. Commercial Activities. The reasonable and good faith interpretation standard extends to the question of whether activities are commercial for purposes of § 414(d). However, for purposes of section III.A.1, it is not a reasonable and good faith interpretation of section 906(a)(1) of PPA ‘06 that an ITG plan is a governmental plan if employees who perform the following commercial activities continue to accrue benefits under the ITG plan. These are employees who are employed by a hotel, casino, service station, convenience store, or marina operated by the ITG from the first day of the first plan year beginning on or after August 17, 2006 (disregarding employees substantially all of whose services as an employee of the ITG are in the performance of essential governmental functions but not in the performance of services for a hotel, casino, service station, convenience store, or marina operated by the ITG).

B. Relief for Mixed ITG plans that Cover Both Governmental and Commercial Employees

Some ITG plans (“mixed ITG plans”) provide benefits both to employees substantially all of whose work is in essential governmental functions that are not commercial activities (“governmental ITG employees”) and to employees who perform commercial activities (“commercial ITG employees”). Furthermore, section 906(a)(1) of PPA ‘06 is effective for some ITG plans soon after its enactment. The IRS and the Department of the Treasury recognize that mixed ITG plans may have substantial difficulty in complying in operation with this provision by the provision’s effective date. Accordingly, this section III.B provides guidance under which, until September 30, 2007, an ITG plan for commercial ITG employees will be treated as a continuation of the mixed ITG plan.

From the first day of the first plan year beginning on or after August 17, 2006, an existing mixed ITG plan will be treated for that plan year as satisfying the reasonable and good faith compliance standard for transitional relief under this notice if, by September 30, 2007, it takes the following steps to provide coverage for governmental ITG employees and commercial ITG employees under separate ITG plans. If an existing mixed ITG plan freezes benefits for the commercial ITG employees, and adopts a new plan covering those commercial ITG employees, in accordance with the steps below, the new ITG plan covering the commercial ITG employees will be treated as a continuation of the relevant portion of the mixed ITG plan that covered the commercial ITG employees prior to the first day of the first plan year beginning on or after August 17, 2006. These steps are:

(1) not later than September 30, 2007, the ITG adopts a separate plan covering commercial ITG employees and that plan complies with the applicable qualification rules under § 401(a) for plans that are not governmental plans under § 414(d) effective as of the first day of the first plan year beginning on or after August 17, 2006;
(2) the ITG takes action, not later than September 30, 2007, to freeze benefit accruals under the mixed ITG plan for commercial ITG employees (including commercial ITG employees who perform services for a hotel, casino, service station, convenience store, or marina operated by the ITG), effective as of the first day of the first plan year beginning on or after August 17, 2006; and

(3) there is no reduction in the benefit formula provided to participants in the continuing commercial ITG plan for the first plan year beginning on or after August 17, 2006 (i.e., the level of accruals or nonelective contributions (including matching contributions) under that plan is not reduced for this year).

This relief applies even if benefits for commercial ITG employees for service before the first day of the first plan year beginning on or after August 17, 2006 are retained under the ITG plan covering governmental employees.

C. Example

The following example illustrates the relief provided in A. and B. of this section III.

Example.  (i) Facts. An ITG maintains a mixed ITG plan (Plan A) for its employees. Plan A covers governmental ITG employees substantially all of whose services are in the performance of essential governmental functions that are not commercial activities, and also commercial ITG employees, i.e., employees whose services are for commercial activities (such as a hotel, casino, service station, convenience store, or marina operated by the ITG). The first day of Plan A’s plan year is October 1. Accordingly, section 906(a)(1) of PPA ’06 is effective for Plan A on October 1, 2006.

(ii) Reasonable and good faith compliance. In order to comply with the requirements of section 906(a)(1) of PPA ’06 to be a governmental plan, action is taken by the ITG on July 1, 2007, to freeze benefits under Plan A with respect to the commercial ITG employees, as of September 30, 2006, so that Plan A only provides benefits for the commercial ITG employees for years of service before October 1, 2006. A continuing plan (Plan B) is adopted on July 1, 2007, effective as of October 1, 2006, the terms of which are the same as Plan A, but which only applies to the commercial ITG employees. Since October 1, 2006, Plan B provides the same level of benefits as were provided under Plan A before October 1, 2006, and Plan B complies with the qualification requirements for plans that are not governmental plans (including the operations of Plan B being consistent with the terms of Plan B). Accordingly, Plan B is treated as a continuation of Plan A from and after October 1, 2006.

(iii) Alternative reasonable and good faith compliance. As an alternative to the action under (ii) of this Example, the ITG takes action on July 1, 2007, effective as of October 1, 2006, to spin off all (or a portion) of the assets and liabilities of Plan A with respect to commercial ITG employees as a separate Plan B for service from and after
October 1, 2006. Since October 1, 2006, Plan B provides the same level of benefits as were provided under Plan A before October 1, 2006, and Plan B (including benefits for service before October 1, 2006) complies with the qualification requirements for plans that are not governmental plans beginning on October 1, 2006 (including the operations of Plan B being consistent with the terms of Plan B). Accordingly, Plan B is treated as a continuation of Plan A from and after October 1, 2006.

D. Definition of Essential Governmental Function

The definition of an essential governmental function under § 7871(e) of the Code for purposes of determining the availability of tax-exempt bond financing for an ITG (including the summary of which activities are considered an essential governmental function customarily performed by State and local governments) described in the advance notice of proposed rulemaking under § 7871 published by the IRS on August 9, 2006\(^3\) will be considered a reasonable and good faith interpretation of what constitutes an essential government function under § 414(d).

E. Relief Only Applies Pending Further Guidance

The relief provided in this section III applies pending the issuance of further guidance relating to § 414(d), including the amendment made by section 906(a)(1) of PPA ’06.

IV. Request for Comments

The IRS and the Department of the Treasury request public comments on issues relating to the amendment made by section 906(a)(1) of PPA ’06, including transitional issues not addressed in this notice (such as issues for ITG plans with a cash or deferred arrangement under § 401(k)). Written comments should be submitted by January 22, 2007. Send submissions to: CC:PA:LPD:PR (Notice 2006-89), room 5203, Internal Revenue Service, POB 7604, Ben Franklin Station, Washington, DC 20044. Submissions may be hand delivered Monday through Friday between the hours of 8 a.m. and 4:30 p.m. to: Crystal Mall 4 Building, 1901 S. Bell St., room 108, Arlington, VA 22202. Alternatively, taxpayers may submit comments electronically to notice.comments@irs_counsel.treas.gov (Notice 2006-89).

Drafting Information

The principal author of this notice is Ingrid Grinde of the Employee Plans, Tax Exempt and Government Entities Division. For further information regarding this notice, please contact the Employee Plans taxpayer assistance telephone service at (877) 829-5500 (a toll-free number) between the hours of 8:00 am and 6:30 pm Eastern Time, Monday through Friday. Ms. Grinde may be reached at (202) 283-9888 (not a toll-free number).

\(^3\) Advance notice of proposed rulemaking, Reg – 118788-06, 71 Fed. Reg. 45474 (August 9, 2006).