

INTERNAL REVENUE SERVICE

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February 22, 2000.

Plan =

Trust =

Employer =

State X =

This is in response to your letter dated August 17, 1999, on behalf of the Employer requesting a ruling on the federal tax consequences of the Plan and Trust. The Employer intends the Plan to be an eligible deferred compensation plan under section 457 of the Internal Revenue Code of 1986 (the "Code"). It is represented that the Employer is a political subdivision of State X and is an employer that is a state or local governmental entity as described in section 457(e)(1)(A).

The Employer established the Plan in 1979 for the benefit of eligible employees. Only executive employees may participate in the Plan. Under the Plan a participant may defer compensation by filing a salary deferral agreement that shall take effect on the first day of the first calendar month following its filing with the Employer. The Plan provides for a maximum amount that may be deferred by a participant in any taxable year and for a catch-up computation for amounts deferred for one or more of the

participant's last three taxable years ending before normal retirement age under the Plan. The amounts that may be deferred under the annual maximum limitation and the catch-up provision are within the limitations set out in section 457 of the Code.

The Plan permits payment of plan benefits upon termination of employment, death, or an unforeseeable emergency. Plan benefits will be paid out in annual installments over a period of one to ten years. The participant may designate the period of years for payout of the annual installments. The election must be made during the twelve months prior to the participant's termination of employment. If the participant fails to make a timely election concerning distribution of the deferred amounts, distributions are made at the time and in the manner prescribed by the Plan. The manner and time of benefits must meet the distribution requirements of section 401(a)(9) and 457(d)(2) of the Code.

The Plan allows segregation of accounts on behalf of and payments to an ex-spouse, or an ex-spouse's beneficiary, pursuant to a court order. The Plan provides that no distribution may be made to an ex-spouse, or an ex-spouse's beneficiary that may violate section 457(d)(1)(A) of the Code.

The Plan, in accordance with section 457(e)(9)(A) of the Code, includes a provision permitting an in-service distribution of \$5,000.00 or less from a participant's account provided that 1) the total amount payable to the participant under the Plan does not exceed the dollar limit under section 411(a)(11) (currently \$5,000), 2) the participant had not previously received an in-service distribution of the total payable to him or her under the Plan, 3) no amount had been deferred under the Plan for the participant during the two-year period ending on the date of such in-service distribution and 4) the participant has elected to receive the distribution.

The Plan further provides that all amounts of compensation deferred pursuant to the Plan, all property and rights purchased with such amounts and all income attributable to such amounts, property, or rights shall be held in trust for the exclusive benefit of participants and beneficiaries under the Plan. The trust under the Plan was established pursuant to a written agreement that is represented to be a valid trust under the laws of State X.

The rights of any participant, or any other person, to payments pursuant to the Plan are not subject in any manner to anticipation, assignment, pledge or charge in whole or in part, either directly or by operation of law or otherwise, including but without limitation, execution, levy, garnishment, attachment, pledge, bankruptcy, or in any other manner, but excluding devolution by death or mental incompetency or assignment by reason of divorce or legal separation from his or her spouse.

The terms of the Trust make it impossible prior to the satisfaction of all liabilities with respect to participants and their beneficiaries for any part of the assets and income

of the trust to be used for, or diverted to, purposes other than the exclusive benefit of participants and their beneficiaries.

Section 457 of the Code provides rules for the deferral of compensation by an individual participant in an eligible deferred compensation plan (as defined in section 457(b)).

Section 457(a) provides that in the case of a participant in an eligible deferred compensation plan, any amount of compensation deferred under the plan and any income attributable to the amounts so deferred shall be includible in gross income only for the taxable year in which such compensation or other income is paid or otherwise made available to the participant or beneficiary.

Section 457(b)(5) prescribes that an eligible deferred compensation plan must meet the distribution requirements of section 457(d).

Section 457(d)(1)(A) provides that for a section 457 plan to be an eligible plan, the plan must have distribution requirements providing that under the plan amounts will not be made available to participants or beneficiaries earlier than i) the calendar year in which the participant attains age 70 ½, ii) when the participant is separated from service with the employer, or iii) when the participant is faced with an unforeseeable emergency as determined under Treasury regulations. However, section 401(a)(9)(C)(i) generally allows plans to postpone the required beginning date until April 1 of the calendar year following the later of the calendar year in which the employee retires or in which he attains age 70 ½.

A basic requirement prescribed by section 457(b)(5) is that an eligible section 457 plan must meet the section 457(d) distribution requirements described above in order to retain its tax-deferred eligible status. A section 457 plan would violate these provisions of section 457(b)(5) and the regulations thereunder if the participant or anyone else received a distribution earlier than the earliest date established in section 457(d)(1)(A).

Section 457(e)(9)(A) provides that the total amount payable to a participant under the plan will not be treated as made available merely because the participant may elect to receive such amount (or the plan may distribute such amount without the participant's consent) if (i) such amount does not exceed \$5,000, and (ii) such amount may be distributed only if--(I) no amount has been deferred under the plan with respect to such participant during the 2-year period ending on the date of the distribution, and (II) there has been no prior distribution under the plan to such participant under this option.

Section 1.457-2(h)(4) of the Income Tax Regulations defines an unforeseeable

emergency as severe financial hardship to the participant resulting from a sudden and unexpected illness or accident of the participant or of a dependent, loss of the participant's property due to casualty, or other similar extraordinary and unforeseeable circumstances arising as a result of events beyond the control of the participant.

Section 457(g)(1) provides that a plan maintained by an eligible governmental employer shall not be treated as an eligible deferred compensation plan unless all assets and rights purchased with such deferred compensation amounts and all income attributable to such amounts, property, or rights of the plan are held in trust for the exclusive benefit of participants and their beneficiaries.

Section 457(g)(2) provides that a trust described in section 457(g)(1) shall be treated as an organization exempt from tax under section 501(a). Section 457(g)(2)(B) provides that the amounts in the trust are treated as includible in the gross income of participants and beneficiaries only to the extent, and at the time, provided in section 457.

Under the terms of the Plan and trust, the trustee must hold all of the section 457(b) plan assets for the exclusive benefit of the participants and their beneficiaries, and all amounts deferred under the Plan must be transferred to a trust meeting the requirements of section 457(g) of the Code within an administratively reasonable time period.

Based upon the provisions of the Plan and Trust summarized above and provided that the Plan is amended as proposed in your letter of January 25, 2000, we conclude as follows:

1. The Plan established by Employer is an eligible deferred compensation plan as defined in section 457(b) of the Internal Revenue Code of 1986. All assets and income of the Plan described in section 457(b)(6) will be held in trust for the exclusive benefit of participants and their beneficiaries.
2. Amounts of compensation deferred in accordance with the Plan, including any income attributable to the deferred compensation, will be includible in the recipient's gross income for the taxable year or years in which amounts are paid or otherwise made available to a participant or beneficiary in accordance with the terms of the Plan.
3. The Plan will not become an ineligible plan described in section 457(f) solely because its administrator or trustee complies with a domestic relations order requiring the distribution of the benefits of a participant

currently eligible to receive distributions to the alternate payee named in the order to meet the participant's obligations with respect to alimony, support, or division of marital rights.

No opinion is expressed concerning the timing of the inclusion in income of amounts deferred under any deferred compensation plan other than the Plan described above. This ruling applies only to deferrals made after the date this ruling is issued. If the Plan is significantly modified, this ruling will not necessarily remain applicable. This ruling applies to the Plan submitted on August 17, 1999, as amended by the Third Amendment to the Restated Salt River Project Agricultural Improvement and Power District Executive Salary Deferral submitted as additional information on January 25, 2000. Section 6110(k)(3) of the Internal Revenue Code provides that it may not be used or cited as precedent.

Temporary or final regulations pertaining to one or more of the issues addressed in this ruling have not yet been adopted. Therefore, this ruling may be modified or revoked if the adopted temporary or final regulations are inconsistent with any conclusion in the ruling. See section 12.04 of Rev. Proc. 2000-1, 2000-1 I.R.B. 4, 46. However, when the criteria in section 12.05 of Rev. Proc. 2000-1 are satisfied, a ruling is not revoked or modified retroactively except in rare or unusual circumstances.

Sincerely,

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Office of the Associate
Chief Counsel
(Employee Benefits and
Exempt Organizations)

Enclosure:

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