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Person To Contact:
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Date:
June 08, 2015

Employers A =

Plan X =
Excess Plan P =
Board B =
City C =
State S =

Dear :

This letter is in response to your ruling request, submitted by your authorized representative on your behalf, dated January 29, 2014, and supplemented by correspondence dated March 16, 2015, and April 24, 2015, with respect to the applicability of section 415(m) of the Internal Revenue Code ("Code") to an excess benefit plan ("Excess Plan P") and the related federal tax consequences.

The following facts and representations have been submitted under penalties of perjury in support of your request:

Plan X is a defined benefit contributory pension plan established by State S legislation which provides pension benefits to the employees of four City C employers, namely, Employers A. Plan X is governmental plan as described in section 414(d), and is intended to meet the qualification requirements of section 401(a). Employee contributions to Plan X are mandatory for all employees of Employers A and are equal to a fixed percentage of each participant's compensation.

Plan X is administered by Board B which consists of five members including City C auditor, two representatives elected by participants in Plan X, one member appointed by

City C manager and, one member who is chosen by the other four members of Board B. Board B members serve three year terms.

Board B adopted Excess Plan P on December 2, 2013. Excess Plan P is intended to be a qualified governmental excess benefit arrangement within the meaning of section 415(m). The purpose of Excess Plan P is solely to provide the portion of a participant's retirement benefit that would otherwise have been payable by Plan X, except for the limitations of section 415(b).

Employees who participate in Plan X will become eligible for benefits from Excess Plan P if their retirement benefit as calculated under the Plan X benefit formula is limited by section 415(b) as that section applies to government plans. Participation in Excess Plan P is mandatory and automatic for all participants in Plan X whose retirement benefits from Plan X are limited by section 415(b).

Excess Plan P provides that a participant will receive a benefit equal to the amount of retirement income that would have been payable to, or with respect to, a participant that could not be paid by Plan X because of the application of the limitations on the participant's retirement income under section 415(b). An excess benefit under Excess Plan P will be paid only if and to the extent the participant is receiving retirement benefits from Plan X. Participation in Excess Plan P will cease for any plan year in which the participant's benefit under Plan X does not exceed the requisite limitations of section 415(b), or if all benefit obligations under Excess Plan P to the retired participant or beneficiary have been satisfied. The form of the benefits paid to a participant from Excess Plan P will be the same form as the participant's retirement benefit under Plan X and will be paid commencing during or with the month in which all monthly payments of retirement benefits under Plan X, as limited by section 415(b), are paid.

Under the terms of Excess Plan P, no election is provided to a participant to defer compensation under Excess Plan P, whether directly or indirectly. In addition, under the represented facts, there will be no employee contributions to Excess Plan P.
Excess Plan P will be administered by Board B. Board B has established a trust fund to hold the employers' contributions intended to pay excess benefits to participants as set forth in Excess Plan P. The assets of the trust fund are separate and apart from the funds of Plan X and will not be commingled with the funds of Plan X. The trust fund is designed as a grantor trust within the meaning of sections 671 through 679. The trustees of this separate trust fund will be members of Board B.

Excess Plan P will be funded on a pay-as-you-go basis. Board B will determine the amount necessary to pay the excess benefits under Excess Plan P for each plan year. The required contribution will be the aggregate of the excess benefits payable to all affected participants for such plan year plus an amount determined by Board B to be a necessary and reasonable expense of administering Excess Plan P. Each employer, in

determining the amount of appropriations necessary to fund Plan X, will also appropriate the amount necessary to fund Excess Plan P. The amount so determined will be withheld from appropriations to Plan X before being credited to Plan X and deposited into the trust fund of Excess Plan P. Under no circumstances will appropriations to fund excess benefits be credited to Plan X. Any contributions not used to pay the excess benefits for a current year, together with any income accruing to the trust fund, will be used to pay the administrative expenses of Excess Plan P for the plan year. Any contributions not so used that remain after the payment of administration expenses will be used to fund administrative expenses or excess benefits in future years.

Based upon the facts and representations stated above, the following rulings are requested:

1. Excess Plan P establishes a qualified governmental excess benefit arrangement within the meaning of section 415(m).

2. The benefits payable under Excess Plan P will be includible in gross income for the taxable year or years in which such benefits are paid or otherwise made available to a participant or a participant's beneficiary in accordance with the terms of Excess Plan P.

3. Income accruing to Excess Plan P is exempt from federal income tax under sections 115 and 415(m)(1) as income derived from the exercise of an essential governmental function.

Section 415(b) and § 1.415(b)-1 of the Income Tax Regulations ("Regulations") set forth the limitations on annual benefits for participants in defined benefit plans.

Section 415(m)(1) provides that, in determining whether a governmental plan (as defined in section 414(d)) meets the benefit limitations of section 415, benefits provided under a qualified governmental excess benefit arrangement shall not be taken into account. Section 415(m)(1) also states that income accruing to a governmental plan (or to a trust that is maintained solely for the purpose of providing benefits under a qualified governmental excess benefit arrangement) shall constitute income derived from the exercise of an essential governmental function upon which such governmental plan (or trust) shall be exempt from tax under section 115.

Section 415(m)(2) describes the tax treatment of benefits payable under a qualified governmental excess benefit arrangement. Under section 415(m)(2), the taxable year or years for which amounts in respect of a qualified excess benefit arrangement are includable in gross income by a participant, and the treatment of such amounts when so includible by the participant, are determined as if such qualified governmental excess benefit arrangement were treated as a plan for the deferral of compensation that is

maintained by a corporation not exempt from tax and which does not meet the requirements for qualification under section 401.

Section 415(m)(3) defines a qualified governmental excess benefit arrangement as a portion of a governmental plan that meets the following three requirements:

(A) Such portion is maintained solely for the purpose of providing to participants in the plan that part of the participant's annual benefit otherwise payable under the terms of the plan that exceeds the limitations on benefits imposed by section 415 ("excess benefits");
(B) Under such portion no election is provided at any time to the participant (directly or indirectly) to defer compensation; and
(C) Excess benefits are not paid from a trust forming a part of such governmental plan unless such trust is maintained solely for the purpose of providing such benefits.

With respect to your first requested ruling, Excess Plan P was adopted by Board B as a part of Plan X. Your authorized representatives have represented that Plan X is a governmental plan as described in section 414(d) and that the only purpose of Excess Plan P is to provide affected employees who are participants in Plan X that portion of their benefits that would otherwise be payable under the terms of Plan X except for the limitations on benefits imposed by section 415(b), as applicable to governmental plans. The terms of Excess Plan P limit participation to participants in Plan X for whom benefits would exceed the limits of section 415. Therefore, we have determined that Excess Plan P is a portion of a governmental plan which is maintained solely for the purpose of providing to employees of Employers A who participate in Plan X that part of the participants' benefits otherwise payable under the terms of Plan X that exceed the section 415 limits, and, as such, meets the requirements of section 415(m)(3)(A).

Your authorized representatives have stated that participation in Excess Plan P is required for all participants or beneficiaries of Plan X whose benefits are limited by section 415(b) and commences automatically each plan year that a participant or beneficiary has an excess benefit, and that there are no employee contributions to Excess Plan P. Your representatives also assert that no direct or indirect election to defer compensation is provided to any participant in Excess Plan P. Thus, we have determined that no direct or indirect election is provided at any time to participants to defer compensation, and accordingly, the requirements of section 415(m)(3)(B) are met.

Section 415(m)(3)(C) requires that the trust from which the excess benefits are paid must not form a part of the governmental plan which contains the excess benefit arrangement, unless such trust is maintained solely for the purpose of providing such benefits. In this case, Excess Plan P will be funded on a pay-as-you-go basis. Board B established a trust fund for the segregation of assets related to Excess Plan P which is maintained separately from Plan X. This trust fund was established solely for the

purpose of holding employer contributions intended to pay excess benefits to affected Plan X participants and beneficiaries. Contributions to the trust fund will consist only of the amounts required to pay the excess benefits and administrative expenses for the plan year. Any contributions not used to pay the excess benefits for a current plan year, together with any income accruing to the trust fund, will be used to pay the administrative expenses of Excess Plan P for the plan year. Any contributions not so used that remain after the payment of administrative expenses will be used to fund excess benefits of participants or pay administrative expenses in future years. Therefore, we have determined that the requirements of section 415(m)(3)(C) are met.

Since Excess Plan P satisfies all of the requirements of section 415(m)(3), we conclude, with respect to your first ruling request, that Excess plan P is a qualified governmental excess benefit arrangement within the meaning of section 415(m).

Your second ruling request asks whether the benefits payable under Excess Plan P will be includible in gross income for the taxable year or years in which such benefits are paid or otherwise made available to a participant or a participant's beneficiary in accordance with the terms of Excess Plan P. In response to your first ruling request, we determined that Excess Plan P meets the legal requirements of section 415(m) and, therefore, constitutes a qualified governmental excess benefit arrangement. Accordingly, under section 415(m)(2), the tax treatment of the amounts distributed under Excess Plan P to the participants is determined as if such qualified governmental excess benefit arrangement were a plan for the deferral of compensation which is maintained by a corporation not exempt from tax and which does not meet the requirements for qualification under section 401.

Section 83(a) provides the rules for inclusion in gross income of the value of property transferred to an employee as compensation for his or her services. The excess of the fair market value of property so transferred over the amount paid for the property is includible in the gross income of the person who performed the services for the first taxable year in which the property becomes transferable or is not subject to a substantial risk of forfeiture.

Section 1.83-3(e) defines the term "property" as including real and personal property other than money or an unfunded and unsecured promise to pay money or property in the future. Under § 1.83-3(e), property also includes a beneficial interest in assets (including money) transferred or set aside from claims of the transferor's creditors, for example, in a trust or escrow account.

Section 402(b) provides that contributions made by an employer to an employee's trust that is not exempt from tax under section 501(a) are included in the employee's gross income in accordance with section 83, except that the value of the employee's interest in the trust will be substituted for the fair market value of the property in applying section 83. Under § 1.402(b)-1(a)(1), an employer's contributions to a nonexempt employee's

trust are included as compensation in the employee's gross income for the taxable year in which the contribution is made, but only to the extent that the employee's interest in such contribution is substantially vested, as defined in the Regulations under section 83.

Section 451(a) and § 1.451-1(a) provide that an item of gross income is includible in gross income for the taxable year in which actually or constructively received by a taxpayer using the cash receipts and disbursements method of accounting. Under § 1.451-2(a), income is constructively received in the taxable year during which it is credited to a taxpayer's account, set apart, or otherwise made available so that the taxpayer may draw on it at any time. However, § 1.451-2(a) further provides that income is not constructively received if the taxpayer's control of its receipt is subject to substantial limitations or restrictions.

The Internal Revenue Service (IRS) has also addressed the issue of constructive receipt as it applies to nonqualified plans of deferred compensation, including excess benefit plans, in various revenue rulings. In Rev. Rul. 60-31, Situations 1-3, the IRS held that a mere promise to pay, not represented by notes or secured in any way, does not constitute receipt of income by a cash basis taxpayer. Rev. Rul. 60-31, 1960-1 C.B. 174, as modified by Rev. Rul. 64-279, 1964-2 C.B. 121, and Rev. Rul. 70-435, 1970-2 C.B. 100; see also Rev. Rul. 69-650, 1969-2 C.B. 106, Rev. Rul. 69-649, 1969-2 C.B. 106; and Rev. Rul. 71-419, 1971-2 C.B. 220.

Under the economic benefit doctrine, an employee is taxable in a year in which any economic or financial benefit is conferred upon the employee as compensation. Sproull v. Commissioner, 16 T.C. 244 (1951), aff'd per curiam, 194 F.2d 541 (6th Cir. 1952). An economic benefit is conferred on an employee when assets are unconditionally and irrevocably paid into a fund or trust to be used for the employee's sole benefit. Id. In Rev. Rul. 72-25, 1972-1 C.B. 127, and Rev. Rul. 68-99, 1968-1 C.B. 193, an employee does not receive income as a result of the employer's purchase of an insurance contract to provide a source of funds for deferred compensation because the insurance contract is the employer's asset, subject to the claims of the employer's creditors.

Based on the foregoing, with respect to the second ruling request, we conclude that the benefits payable under Excess Plan P will be includible in gross income for the taxable year or years in which such benefits are paid or otherwise made available to a participant or a participant's beneficiary in accordance with the terms of Excess Plan P.

With respect to your third requested ruling, section 415(m)(1) provides that income accruing to a governmental plan (or to a trust that is maintained solely for the purpose of providing benefits under a qualified governmental excess benefit arrangement) in respect of a qualified governmental excess benefit arrangement will constitute income derived from the exercise of an essential governmental function upon which such governmental plan (or trust) will be exempt from tax under section 115. We have determined, in connection with your first ruling request, that Excess Plan P meets the

legal requirements of section 415(m) for qualified governmental excess benefit arrangements. Therefore, under section 415(m)(1), with respect to your third requested ruling, we conclude that income accruing to Excess Plan P is exempt from federal income tax under sections 115 and 415(m)(1) as income derived from the exercise of an essential governmental function.

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 the trust fund established for the purpose of holding employer contributions intended to pay excess benefits to Excess Plan P participants constitutes a grantor trust under Rev. Proc. 92-64, 1992-33 I.R.B. 11.

This letter assumes that Plan X is and was a governmental plan as described in section 414(d), is and was qualified under section 401, and its related trust is and was exempt from tax under section 501(a) at all relevant times thereto.

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

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

The rulings contained in this letter are 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.

Sincerely,

Jason E. Levine
Senior Tax Law Specialist
Qualified Plans Branch 4
(Tax Exempt & Government Entities)

cc:

bcc: EP Classification
TE/GE Headquarters