

Internal Revenue Service

Department of the Treasury
Washington, DC 20224

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Person To Contact:
, ID No.

Telephone Number:

Refer Reply To:
CC:EEE:EB:QP1
PLR-132632-18

Date:
May 16, 2019

In Re:

Legend:

- Plan =
- State =
- Date 1 =
- Date 2 =
- Date 3 =
- Option 1 =
- Option 2 =

Dear :

This is in response to your request dated October 29, 2018, as supplemented by information dated April 11, 2019, in which your authorized representatives request a private letter ruling on your behalf regarding the application of section 401(a)(9) of the Internal Revenue Code to Plan.

The following facts and representations have been submitted under penalty of perjury in support of the rulings requested:

Plan is a multiple-employer public employee retirement system established by State to provide retirement annuities and other benefits for employees, survivors and other beneficiaries of those employees of State's universities, community colleges, and certain other educational and scientific agencies. Plan provides a qualified defined benefit plan under which there are two benefit options, Option 1 and Option 2. Plan also provides a qualified defined contribution plan. Members of Plan choose one of these three options upon employment with a covered employer. Members who first

become Plan members prior to Date 1, and who are not participants in the defined contribution plan, are referred to as Tier 1 members. Plan represents that the underlying defined benefit and defined contribution plans are qualified plans under section 401(a) and governmental plans within the meaning of section 414(d).

Preliminary Payments

A member who retires after meeting applicable age and service requirements is entitled to a retirement annuity from Plan. A member may specify the date that his or her annuity period begins on his or her retirement application. However, a member's annuity payment period may not begin before the member's termination of employment nor more than one year before the member's retirement application is received by Plan, and must begin by his or her required beginning date under section 401(a)(9). A member's retirement begins with the beginning of his or her annuity payment period.

Plan requires an administrative period following a member's retirement to calculate his or her retirement annuity, which typically takes three weeks to six months to complete. For the period that begins on the member's effective retirement date and ends when the retirement annuity calculation is finalized and paid, Plan provides members with a portion of their retirement annuity. These preliminary payments are provided to reduce the financial hardship on retirees during the calculation process, as Plan-covered employment is not covered by Social Security, and many retirees are without any other source of retirement income. The preliminary payments are calculated as a percentage of the member's estimated retirement annuity amount, with certain adjustments.

If a member's retirement application is received at least 90 days before his or her effective retirement date (the first day of the member's annuity payment period), the preliminary payments will begin on the first working day of the month following the member's effective retirement date and continue thereafter until Plan completes its calculation of the member's retirement annuity. If a retirement application is received less than 90 days before the member's effective retirement date, the preliminary payments will begin as soon as practicable following the effective retirement date and continue thereafter until Plan completes its calculation of the member's retirement annuity. After Plan finalizes the member's retirement annuity calculation, it reconciles the final retirement annuity amount with the amount of the preliminary payment, and it provides a catch-up payment to the extent that the final retirement annuity amount exceeds the preliminary payment amount, retroactive to the effective retirement date, without interest. Similarly, if the retirement annuity is calculated to be less than the amount of the preliminary payment, overpayments are recouped from future retirement annuity payments, without interest.

Buyout Offered to Tier 1 Members

On Date 2, State legislature amended State law to provide two additional pension payout options under Plan. Plan intends to offer an election to eligible Tier 1 members

to choose a lump sum payment in exchange for a delay and reduction in the cost-of-living increase otherwise applicable to the member's annuity (the "buyout"). Plan provides that Tier 1 members are eligible to receive a retirement annuity in the form of a single life annuity with an annual increase of 3% of the amount payable in the prior year. It is available to eligible members only during the period commencing on the implementation date (as defined by State statute) and ending Date 3. An eligible Tier 1 member who elects the buyout will receive an annual increase of 1.5% of the original amount of the annuity beginning on January 1 following the later of the member's 67th birthday or one year after retirement. The accelerated pension benefit payment is a lump sum payment equal to 70% of the difference between the present value of the 3% compounded annually annual increase and the present value of the 1.5% simple interest annual increase delayed until age 67, determined using actuarial factors that are specified in Plan. The buyout reduces future cost-of-living increases to the member's annuity, but it does not change the beginning retirement annuity amount. Under State law, eligible members must elect the buyout before any retirement annuity is paid. Thus, a buyout is available only to a Tier 1 member who has not yet filed a retirement application to commence his or her retirement annuity.

An eligible Tier 1 member must submit an application for the buyout at the same time that the member submits an application for a retirement annuity. This election for the buyout is based on an estimated annuity payment and estimated buyout amount. Upon the election of an eligible Tier 1 member, Plan is required to calculate the finalized buyout amount and offer the member the opportunity to confirm his or her election of the buyout in a final election. Plan will pay the preliminary payments (as mentioned above) to these members from their effective retirement dates and prior to confirming their buyout elections in the same manner as they are paid to members who are not eligible for the buyout or do not apply for the buyout.

Taxpayer requests the following rulings:

1. An eligible Tier 1 member's final election of the buyout that occurs after the member's effective retirement date, and which is solely due to administrative delay in finalizing the claim for benefits, is not treated as an accelerated annuity payment after benefit commencement that is prohibited under section 401(a)(9) and § 1.401(a)(9)-6, Q&A-1.
2. The payment of a preliminary payment to Tier 1 members who are eligible for the buyout prior to the member's final election of the buyout due solely to administrative delay does not constitute annuity payments that may be accelerated upon election of the buyout in violation of section 401(a)(9) and § 1.401(a)(9)-6, Q&A-1.

Section 401(a)(9) provides that a trust shall not constitute a qualified trust unless the plan provides that the entire interest of each employee (i) will be distributed to such employee not later than the required beginning date, or (ii) will be distributed, beginning

not later than the required beginning date, in accordance with regulations, over the life of such employee or over the lives of such employee and a designated beneficiary (or over a period not extending beyond the life expectancy of such employee or the life expectancy of such employee and a designated beneficiary).

Section 1.401(a)(9)-6, Q&A-1(a) provides that in order to satisfy section 401(a)(9), except as otherwise provided in § 1.401(a)(9)-6, distributions of the employee's entire interest under a defined benefit plan must be paid in the form of periodic annuity payments for the employee's life (or the joint lives of the employee and beneficiary) or over a period certain that does not exceed the maximum length of the period certain determined in accordance with § 1.401(a)(9)-6, Q&A-3. The interval between payments for the annuity must be uniform over the entire distribution period and must not exceed one year. Once payments have commenced over a period, the period may only be changed in accordance with § 1.401(a)(9)-6, Q&A-13. Except as otherwise provided in § 1.401(a)(9)-6 (such as permitted increases described in Q&A-14), all payments (whether paid over an employee's life, joint lives, or a period certain) also must be nonincreasing.

Section 1.401(a)(9)-6, Q&A-1(b) provides that the annuity may be a life annuity (or joint and survivor annuity) with a period certain if the life (or lives, if applicable) and period certain each meet the requirements of § 1.401(a)(9)-6, Q&A-1(a).

Section 1.401(a)(9)-6, Q&A-1(c) provides that annuity payments must commence on or before the employee's required beginning date (within the meaning of § 1.401(a)(9)-2, Q&A-2). The first payment, which must be made on or before the employee's required beginning date, must be the payment which is required for one payment interval. The second payment need not be made until the end of the next payment interval even if that payment interval ends in the next calendar year. Similarly, in the case of distributions commencing after death in accordance with section 401(a)(9)(B)(iii) and (iv), the first payment, which must be made on or before the date determined under Q&A-3(a) or (b) (whichever is applicable) of § 1.401(a)(9)-3, must be the payment which is required for one payment interval. Payment intervals are the periods for which payments are received, e.g., bimonthly, monthly, semi-annually, or annually. All benefit accruals as of the last day of the first distribution calendar year must be included in the calculation of the amount of annuity payments for payment intervals ending on or after the employee's required beginning date.

Section 1.401(a)(9)-6, Q&A-14 provides that except as otherwise provided in this section, all annuity payments (whether paid over an employee's life, joint lives, or a period certain) must be non-increasing or increase only in accordance with one or more of the following:

(1) With an annual percentage increase that does not exceed the percentage increase in an eligible cost-of-living index as defined in paragraph (b) of this A-14 for a 12-month period ending in the year during which the increase occurs or the prior year;

(2) With a percentage increase that occurs at specified times (e.g., at specified ages) and does not exceed the cumulative total of annual percentage increases in an eligible cost-of-living index as defined in paragraph (b) of this A-14 since the annuity starting date, or if later, the date of the most recent percentage increase. However, in cases providing such a cumulative increase, an actuarial increase may not be provided to reflect the fact that increases were not provided in the interim years;

(3) To the extent of the reduction in the amount of the employee's payments to provide for a survivor benefit, but only if there is no longer a survivor benefit because the beneficiary whose life was being used to determine the period described in section 401(a)(9)(A)(ii) over which payments were being made dies or is no longer the employee's beneficiary pursuant to a qualified domestic relations order within the meaning of section 414(p);

(4) To pay increased benefits that result from a plan amendment;

(5) To allow a beneficiary to convert the survivor portion of a joint and survivor annuity into a single sum distribution upon the employee's death; or

(6) To the extent increases are permitted in accordance with paragraph (c) or (d) of this A-14.

With regard to your first requested ruling, under § 1.401(a)(9)-6, Q&A-1(a), the stream of annuity payments received by a Tier 1 member must be nonincreasing once benefits commence. Accordingly, if a Tier 1 member began receiving annuity payments and then was offered an election to convert a portion of the existing stream into a lump sum, the amount of the payments would increase in the year the lump sum payment was received, in violation of § 1.401(a)(9)-6, Q&A-1(a). However, under the facts of this case, the election to receive the buyout occurs with the initial retirement application, at which time a member may elect to receive or reject the buyout. If the member elects the buyout, the buyout calculation is included as part of the overall annuity calculation and is confirmed upon finalization of the calculations. Even though the preliminary payments are paid to the member beginning on the annuity starting date, because the election is made before the annuity starting date, an eligible Tier 1 member's subsequent confirmation of the election of the buyout after the member's effective retirement date, solely due to administrative delay in finalizing the buyout calculations and the claim for benefits, is not treated as an accelerated annuity payment after benefit commencement that is prohibited under section 401(a)(9) and § 1.401(a)(9)-6, Q&A-1.

With regard to your second requested ruling, pursuant to your representations, the monthly preliminary payments are made to each retired member beginning on his or her annuity starting date, and calculated based on his or her estimated monthly retirement amount. The preliminary payments are paid during the administrative period that arises for calculating the final annuity amount and are reconciled when the final amount is

calculated. The reconciliation payments are not additional benefits because the amount of the payments received by the member once the calculation is made equals what would have been paid if equal annuity payments, as determined in the final calculation, had been made starting on the annuity starting date. Therefore, the payment of preliminary payments to Tier 1 members who are eligible for the buyout prior to the member's confirmation of the election of the buyout due solely to administrative delay does not constitute annuity payments that are accelerated upon election of the buyout in violation of section 401(a)(9) and § 1.401(a)(9)-6, Q&A-1.

The rulings contained in this letter are based upon information and representations submitted by your authorized representatives and accompanied by a penalty of perjury statement executed by an appropriate party, as specified in Rev. Proc. 2019-1, 2019-1 I.R.B. 1, § 7.01(16)(b). This office has not verified any of the material submitted in support of the request for ruling, and such material is subject to verification on examination. The Associate office will revoke or modify a letter ruling and apply the revocation retroactively if there has been a misstatement or omission of controlling facts; the facts at the time of the transaction are materially different from the controlling facts on which the ruling was based; or, in the case of a transaction involving a continuing action or series of actions, the controlling facts change during the course of the transaction. See Rev. Proc. 2019-1, § 11.05.

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.

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 each of your authorized representatives.

Sincerely,

Laura B. Warshawsky
Branch Chief
Qualified Plans Branch 1
Office of Associate Chief Counsel
(Employee Benefits, Exempt Organizations, and
Employment Taxes)

cc: