

INTERNAL REVENUE SERVICE
Index No. 457.01-00 457.05-00
457.09-04

Number: **199923010**
Release Date: 6/11/1999

CC:EBEO:1 - PLR-119882-98

March 2, 1999

Entity E =

State S =

Participant P =

Trustee T =

Dear:

This responds to your letter of September 14, 1998 and subsequent correspondence, on behalf of Entity E, requesting a ruling concerning the proposed amended and restated deferred compensation plan (the "Plan") which E intends to be an eligible deferred compensation plan under section 457 of the Internal Revenue Code of 1986. E is represented to be a political subdivision of State S and thus to be an eligible governmental entity described in section 457(e)(1)(A).

The facts presented are as follows. Under the Plan an employee of E, such as Participant P, may elect to defer compensation he or she would have received for services rendered to Entity E until attainment of age 70 ½, death, separation from service with the employer, or until the occurrence of an unforeseeable emergency. Any employee (including non-highly compensated, non-management employees) and independent contractor employed by E may participate in this Plan by signing a participation agreement. The Plan also includes a provision permitting a participant to elect an in-service distribution of \$5,000.00 or less from his or her account in certain limited circumstances set forth thereunder and in accordance with section 457(e)(9)(A). The Plan also includes a provision permitting a participant to make a plan-to-plan transfer under section 457(e)(10) to another eligible section 457(b) plan in certain limited circumstances set forth therein.

The participant's election to defer compensation under the Plan must be filed prior to the beginning of the month in which his or her salary reduction agreement becomes effective. The Plan provides for a maximum amount that may be deferred by a participant in any taxable year and also provides for a catch-up computation for amounts deferred for one or more of the participant's last three taxable years ending before he attains 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 of section 457 including the section 457(c) coordinated deferral provision.

PLR-119882-98

With certain limitations, a participant may elect the manner in which his or her deferred amounts will be distributed. A distribution election must be made prior to the date any such payment must commence to the participant. If the participant fails to make a timely election, distribution will commence at the time and in the manner set forth in the Plan. The manner and time of benefit payout must meet the distribution requirements of sections 401(a)(9) and 457(d) of the Code.

In accordance with section 457(g), the assets of the Plan will be held in a trust established pursuant to a written agreement that constitutes a valid trust under state law. The Plan further provides that, in accordance with section 457(g) of the Code, the trustee of its assets must hold all the section 457 plan's assets for the exclusive benefit of the participants and their beneficiaries, and that all amounts deferred under the Plan must be transferred to the trust within an administratively reasonable time period. To comply with this requirement, all amounts of compensation deferred under the plan are required to be transferred to a subaccount maintained by the plan trustee in the name of the participant not later than 15 business days after the end of the month in which the compensation would otherwise have been paid to the participant. The trustee, T, is represented to be a third-party financial institution. The rights of any participant or beneficiary to payments pursuant to the Plan are generally nonassignable.

The Plan provides that distribution to a former spouse or alternate payee pursuant to a domestic relations order may occur or commence only when the participant himself becomes eligible to receive distributions under the Plan and under section 457(d). If such alternate payee receives rights to amounts in a participant's account under a domestic relations order, the Plan may maintain a bookkeeping account for such beneficiary. The plan administrator may make distributions from such account pursuant to the domestic relations order to the alternate payee at or after the time section 457(d) permits distributions from the participant's account.

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

Section 457(a) of the Code 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).

PLR-119882-98

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.

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(e)(10) provides that a participant is not required to include in gross income any portion of the entire amount payable to such participant solely due to the transfer of such portion from one eligible deferred compensation plan to another eligible deferred compensation plan.

Section 457(f) provides that if a section 457 plan is or becomes an ineligible plan then the deferred compensation shall be included in the gross income of the participant or beneficiary for the first taxable year in which there is no substantial risk of forfeiture of the rights to such compensation, and the tax treatment of any amount made available under such plan to a participant or beneficiary shall be determined under section 72 relating to annuities.

Section 457(g) 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.

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 from the its assets earlier than the earliest date established in section 457(d)(1)(A).

PLR-119882-98

Based upon the facts and representations submitted, the provisions of the revised plan and the amendments summarized above, and the other documents presented, we conclude as follows:

1. The Deferred Compensation Plan established by Entity E, along with the submitted supporting documents, constitutes an eligible deferred compensation plan as defined in section 457(b) of the Internal Revenue Code of 1986. E's Plan remains an eligible plan under section 457(b) even though E may make this plan available to all its employees, including non-highly compensated and non-management employees, since E is an eligible governmental entity.
2. Amounts of compensation deferred in accordance with the Plan, including any income attributable to the deferred compensation, will be includible in gross income for the taxable year or years in which amounts are paid or otherwise made available to a participant, such as P, or beneficiary (including one named in a domestic relations order) in accordance with the terms of the Plan.
3. E's 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 in pay status (currently eligible to receive distributions) under section 457(d)(1)(A) to the alternate payee named in the order (such as the participant's spouse or ex-spouse) to meet the participant's obligations with respect to alimony, support, or division of marital rights.
4. The trust established under E's section 457(b) Plan is treated under section 457(g) as exempt from federal income taxation pursuant to section 501(a). Trustee T is eligible to serve as the trustee of the trust established under E's Plan pursuant to section 457(g).
5. The transfer of any amount from a participant's account in the Plan to another eligible deferred compensation plan will not result in the inclusion in the gross income of the participant of any portion of the entire amount payable to the participant from the account. Section 457(e)(10).

No opinion is expressed concerning the timing of the inclusion in income of amounts deferred under any deferred compensation plan other than E's Plan described above. In addition, this ruling applies only to deferrals made after the date this ruling was issued. If either the Plan, the trust associated with the Plan, or other supporting documents submitted with the ruling request is significantly modified, this ruling will not

PLR-119882-98

necessarily remain applicable. This ruling is directed only to Entity E and to the participants and beneficiaries of its Plan and applies only to the Plan and other documents submitted on September 14, 1998 and revised in accordance with the amendments submitted on December 1, 1998. 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. 99-1, 1999-1 I.R.B. 6, 47. However, when the criteria in section 12.05 of Rev. Proc. 99-1 are satisfied, a ruling is not revoked or modified retroactively except in rare or unusual circumstances.

Sincerely yours,

ROBERT D. PATCHELL
Assistant Chief, Branch 1
Office of the Associate
Chief Counsel
(Employee Benefits and
Exempt Organizations)

Enclosure: