Internal Revenue Service Department of the Treasury

Washington, DC 20224

Significant Index Nos. 401.28-00, 412.01-00, 415.01-00

Person to Contact:

Telephone Number:

Refer Reply to:

OP:E:EP:A:2

Date:

SEP 03 1999

In re: Request for ruling on behalf of

Plan T =

Plan E =

Employer C =

This letter is in response to your request, dated October 26, 1998, for rulings on behalf of Plan T and Employer C related to the creation of an excess benefit plan and its effect on Plan T, and the deductibility of contributions to fund such plan.

Facts

According to the facts as stated, Plan T is a multiemployer defined benefit pension plan that is qualified under section 401(a) of the Internal Revenue Code (Code), with its most recent favorable determination letter dated May 22, 1995. Employer C is one of the employers that maintain Plan T. Plan T has been in existence since May 1962. The contribution rate to fund Plan T is established by the currently effective collective bargaining agreement between the union and the employers who maintain Plan T. A special study by Plan T's actuary determined that if employees retired at relatively early retirement ages (55-57) and received unreduced (subsidized) early retirement benefits, their benefits were likely to be adversely affected under the rules of Code section 415(b). Younger employees who continue to work in the trade on a regular basis might also have their benefits adversely affected by the limitations of Code section 415(b). In response to these projections, the trustees of Plan T decided to create an excess benefit plan, Plan E, to provide those portions of participants' benefits under Plan T that were reduced under the rules of section 415. Plan E will not become effective until favorable responses to the rulings requested herein are

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received from the Internal Revenue Service (Service) with respect to certain issues involving the effect of Plan E on the qualified status of Plan T and the deductibility of contributions to Plan E.

Plan E is designed to provide, on a nonqualified basis, benefits in excess of those permitted to be paid by Plan T by reason of the limitations imposed by section 415. The amount to be paid to participants under Plan E will be increased to reflect FICA taxes due thereon. Plan E is not expected to hold significant assets. Pursuant to the collective bargaining agreement, the amount of benefits to be paid under Plan E in a given month plus FICA taxes and administrative expenses will be remitted to Plan E's administrative manager each month. The amount of benefits to be paid that month will be allocated to separate bookkeeping accounts for those participants who are entitled to receive benefits from Plan E. All amounts received by Plan E, including any trust income, will be allocated to the payment of Plan E expenses and then to pay benefits to Plan E participants each month. All contributions made to Plan E by employers will be allocated and used to pay benefits and defray administrative expenses in the taxable year in which they are contributed. No principal amounts or interest income, if any, will be allowed to accumulate in the Plan E trust. Thus, the trust associated with Plan E will merely act as a passthrough entity for excess benefit payments and related expenses. The administrative manager of Plan T will act as the administrative manager of Plan E.

Thus, a participant's benefit under Plan E is equal to the amount of the participant's benefit under Plan T's benefit formula (before limitation for section 415) in excess of the benefit Plan T can provide to the participant under section 415 (that is, after limitation for section 415). Such amount is to be further increased to reflect the FICA taxes due on such amount, so that the payments to be paid to a Participant, net of FICA taxes, are the same amounts the Participant would receive if the amounts were not subject to FICA taxes.

To fund Plan E, the collective bargaining agreement will be amended. The amendment to the applicable bargaining agreement will not be finalized before a favorable response to the rulings requested herein is received. The amendment to the collective bargaining agreement will modify Plan T's funding as follows.

a. The collective bargaining agreement amendment will require that on a monthly basis Plan T's administrative manager will calculate the amount necessary to pay Plan E's benefits and expenses for the month.

b. Plan T's administrative manager will deduct from the funds received from employers (i.e., the collectively bargained hourly contribution rate), including Employer C, the amount necessary to pay Plan E benefits, FICA taxes, and related administrative expenses. The amount necessary to pay these benefits and expenses will be transmitted to Plan E's trust fund for payment to Plan E participants or for payment of Plan E expenses.

c. All contributions not remitted to Plan E will then be forwarded to the trust fund for Plan T.

Thus, employers of bargaining unit employees (including Employer C) will continue to submit the required employer contributions for each hour worked by each bargaining unit member to the administrative manager of Plan T. Pursuant to the terms of the collective bargaining agreement amendment, a portion of the funds received will be remitted to Plan E and the remainder of the funds will be submitted to Plan T. The only contributions that will be allocated to Plan E are those that are required to be allocated to Plan E by the terms of the collective bargaining agreement. This allocation will always occur before the funds are deposited in any Plan T account. Once contributions are received by Plan T, they cannot be shifted to Plan E.

Ruling Requested

Based on the facts as stated, the following rulings have been requested by Plan T and Employer C.

1. The use of Plan E will not cause Plan T to lose its qualified status under section 401(a) of the Code.

2. The allocation of contributions to Plan E will not cause Plan T to lose its qualified status under section 401(a) of the Code.

3. Any employer contributions allocated to Plan E pursuant to the collective bargaining agreement, if otherwise deductible, will be deductible by the employers under section 404 of the Code.

Applicable Law

Section 3(36) of Title I of the Employee Retirement Income Security Act of 1974 (ERISA) provides that the term "excess benefit plan" means a plan maintained by an employer solely for the purpose of providing benefits for certain employees in excess of the limitations on contributions and benefits imposed by section 415 of the Code on plans to which that section applies, without regard to whether the plan is funded. To the extent that a separable part of a plan (as determined by the Secretary of Labor) maintained by an employer is maintained for such purpose, that part shall be treated as a separate plan which is an excess benefit plan.

Section 401(a)(16) of the Code provides that a qualified plan must not provide for benefits or contributions that exceed the limitations of section 415.

Section 404 of the Code provides deduction rules for contributions of an employer to an employees' trust or annuity plan and compensation under a deferred-payment plan. Section 404(a) provides that, if contributions are paid by an employer to or under a stock bonus, pension, profit-sharing, or annuity plan, or if compensation is paid or accrued on account of any employee under a plan deferring the receipt of such compensation, such contributions or compensation are not deductible under that chapter; but, if they would otherwise be deductible, they shall be deductible under that section, subject, however, to the limitations in that section as to the amounts deductible in any year. Section 404(a)(5) provides that contributions or compensation deferred under a plan not included in section 404(a)(1), (2), or (3), are deductible in the taxable year in which an amount attributable to the contribution is includible in the gross income of the employees participating in the plan, but in the case of a plan in which more than one employee participates, only if separate accounts are maintained for each employee.

Section 412 of the Code provides minimum funding standards that pension plans must satisfy. Section 412(h) provides exceptions to the minimum funding standards of section 412 for certain plans.

Section 415 of the Code provides limitations on benefits and contributions that may be provided under qualified plans. Section 415(b) provides limitations that qualified defined benefit plans must satisfy. Section 415(b)(1) provides, in general, that the annual benefit a participant can receive under a qualified defined benefit plan must not exceed the lesser of a specified dollar amount or 100 percent of the participant's average compensation for his high 3 years. The specified dollar amount effective January 1, 1999, is $130,000.

Section 1.404(a)-12(b) of the Income Tax Regulations provides that, in general, a deduction is allowable for a contribution only in the taxable year of the employer in which or with which ends the taxable year of an employee in which an amount attributable to such contribution is includible in the employee's gross income as compensation, and then only to the extent allowable under Code section 404(a). In the case of a funded plan under which more than one employee participates, no deduction is allowable under Code section 404(a)(5) for any contribution unless separate accounts are maintained for each employee.

Section 1.414(l)-1(b)(1) of the Income Tax Regulations provides that, for purposes of that section, a plan is a "single plan" if and only if, on an ongoing basis, all of the plan assets are available to pay benefits to employees who are covered by the plan and their beneficiaries.

Rationale

Code section 401(a)(16) provides that a qualified plan must satisfy section 415. Section 415(b) provides limitations that benefits provided under a qualified defined benefit plan must satisfy. Thus, where a participant's benefit under Plan T's benefit formula exceeds the section 415(b) limitation applicable to the participant, adjusted as necessary for the commencement age and the form in which the benefit will be paid, the participant's benefit under Plan T must be limited (reduced) so that it does not exceed such limitation.

Section 3(36) of Title I of ERISA provides that an excess benefit plan is a plan maintained by an employer solely for the purpose of providing benefits for certain employees in excess of the section 415 limitation applicable to the employee, without regard to whether the plan is funded. Plan E is intended to be an excess benefit plan under section 3(36) of ERISA.

Section 1.414(l)-1(b)(1) of the regulations provides that a plan is a single plan, for purposes of that section, if and only if all of the plan assets are available to pay benefits to participants and beneficiaries. The assets of Plan T are not available to pay benefits under Plan E, and assets of Plan E are not available to pay benefits under Plan T. Therefore, Plan T and Plan E do not constitute a single plan. Plan E is separate from Plan T and provides benefits on a nonqualified basis which supplement the benefits that certain participants in Plan T receive from Plan T. Furthermore, the benefit provided to a participant under Plan E cannot be provided by Plan T because it would cause the participant's Plan T benefit to exceed the limitations of section 415. Thus, the existence of Plan E, an excess benefit plan, does not affect the qualified status of Plan T.

The contribution rate for employers (including Employer C) who sponsor Plan T and Plan E is established as part of the collective bargaining agreement. In order to provide promised benefits under Plan T and Plan E, an actuary must determine the amounts necessary to provide such benefits. Additionally, because Plan T is a qualified defined benefit plan subject to Code section 412, the actuary must determine the contributions required to avoid a funding deficiency in Plan T's funding standard account for each plan year. Such actuarial calculations are independent of the contribution rate established by the collective bargaining agreement. Furthermore, the minimum funding requirements for Plan T are independent of the amounts contributed to Plan E. Thus, the allocation of employer contributions to Plan E pursuant to the collective bargaining agreement will not affect the qualified status of Plan T. Note that, in general, whether or not a plan is qualified under section 401(a) of the Code is determined under the rules of section 401(a). The allocation of contributions to Plan E will not, by itself, cause Plan T to fail to satisfy section 401(a).

Section 404(a) of the Code provides the general deduction timing rules applicable to a stock bonus plan, pension, profit sharing, or annuity plan, or if compensation is paid or accrued on account of any employee under a plan or arrangement for deferring compensation, regardless of the

Code section under which the amounts might otherwise be deductible. Pursuant to section 404(a)(5), contributions or compensation deferred under a nonqualified plan or arrangement, if otherwise deductible, are deductible in the taxable year in which an amount attributable to the contribution are includible in the gross income of the employees participating in the plan, but in the case of a plan in which more than one employee participates, only if separate accounts are maintained for each employee.

Section 1.404(a)-12(b)(3) of the regulations provides that a deduction is allowable for contributions paid only in the taxable year in which or with which ends the taxable year of an employee in which an amount attributable to the contribution is includible in his or her income as compensation, and then only to the extent allowable under section 404(a).

Because employees who participate in Plan E are fully vested in their benefits when employer contributions are made and separate accounts are maintained for each employee, each employer who participates in Plan E is entitled to a deduction under section 404(a)(5) of the Code in an amount equal to the amount included in income by their respective employees, assuming all other requirements for deductibility are met. The deduction is allowable in the taxable year in which or with which ends the taxable year of the employee in which the amount is includible in the employee's income as compensation.

Holdings

1. The use of Plan E will not cause Plan T to lose its qualified status under section 401(a) of the Code.

2. The allocation of contributions to Plan E will not cause Plan T to lose its qualified status under section 401(a) of the Code.

3. Any employer contributions allocated to Plan E pursuant to the collective bargaining agreement, if otherwise deductible, will be deductible by the employers under section 404 of the Code.

Note

This ruling is directed only to the organizations that requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited by others as precedent.

This letter does not consider the more general issue of Plan T's qualified status, specifically, whether Plan T complies with all the Code requirements for qualification. This letter addresses only the impact (if any) of the adoption and funding of Plan E on the purportedly otherwise qualified status of Plan T. Additionally, except as specifically ruled above, no opinion is expressed regarding the subject transaction under any other provision of the Code, including the consequences to participants under section 83 and 402(b) of the Code. Moreover, we express no opinion regarding the federal employment tax aspects of the above-described transaction.

Sincerely yours,

Martin L. Pippins

Martin L. Pippins
Acting Chief, Actuarial Branch 2

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