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Internal Revenue Service

Department of the Treasury

Washington, DC 20224

Uniform Issue List : 403.00-00

Contact Person: OP:E:EP:T4

Telephone Number:

In Reference to:

Date: SEP 30 1999

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Legend:

Employer M: =

Plan X: =

This is in response to a ruling request dated August 4, 1998, as supplemented by correspondence dated January 25, 1999; September 2, 1999; and September 9, 1999, submitted on your behalf by your authorized representative, with respect to an arrangement described under section 403(b)(1) of the Internal Revenue Code ("the Code").

The following facts and representations have been submitted on your behalf:

Employer M is an organization described in section 501(c)(3) of the Code. Employer M established Plan X for the benefit of the employees of Employer M.

Under Plan X, participants may elect to invest funds in various insurance-company annuity contracts, as well as a variety of custodial account agreements.

Pursuant to section 3.1 of Plan X, all employees, other than those permitted to be excluded under section 403(b)(12), may participate in Plan X upon completion of a salary reduction agreement.

Pursuant to sections 2.11 and 4.2 of Plan X, participations are, as a condition of employment, required to make contributions to Plan X. Required Participant Contributions are deducted from the amount of compensation otherwise payable to the participant; however, they are a mandatory condition of employment and are not treated under the Plan as elective deferrals if they were a condition of employment when made.

The three following types of contributions may be made to Plan X on behalf of a participant: (1) employee voluntary salary reduction contributions as provided for by section 4.1 of the Plan, (2) employee mandatory contributions required by section 4.2 of the Plan, and (3) employer matching contributions under section 4.3 of the Plan.

Pursuant to sections 5.2, 5.3, 6.1, and 6.2, of Plan X, distributions from the Plan may be made only upon attainment of age 59½, hardship, separation from service, or death.

Salary reduction contributions must be limited to the lesser of the maximum exclusion allowance in accordance with section 403(b)(2) or the limitations under section 415(c). Under section 4.4 of Plan X, all contributions under the Plan are limited to the amount of the "exclusion allowance" as set forth under section 403(b)(2) of the Code, and shall not exceed the limitations under Code section 415 on the participant's "annual additions" for the Plan Year taking into account the special elections under Code section 415(c)(4) where applicable.

Under section 4.6 of Plan X, all amounts allocated to a participant's annuity contract will at all times be fully vested and nonforfeitable.

Under section 6.3 of Plan X, distributions from the Plan will be made no later than the required beginning date provided in section 401(a)(9) of the Code .

Section 6.4 of Plan X provides that a distributee receiving an eligible rollover distribution under the Plan may elect to have the distribution rolled over in a direct rollover to an eligible retirement plan.

Based upon the foregoing facts and representations, you request rulings that:

1. Plan X satisfies the requirements of section 403(b) of the Code;

2. Contributions, including elective deferrals, under the Plan are not includible in the income of the participants so long as the amounts do not exceed the limitations of sections 402(g), 403(b), or 415;

3. All distributions from the Plan will be taxed under sections 72 and 403(b)(1); and

4. Pre-tax contributions required to be made as a condition of employment are not subject to the section 402(g) limit.

Section 403(b)(1) of the Code provides, in part, that amounts contributed by an employer to purchase an annuity contract for an employee are excludable from the gross income of the employee in the year contributed to the extent of the applicable "exclusion allowance", provided (1) the employee performs services for an employer which is exempt from tax under section 501(a) of the Code as an organization described in section 501(c)(3), or the employee performs services for an educational institution (as defined in section 170(b)(1)(A)(ii) of the Code) which is a state, a political subdivision of a state, or an agency or instrumentality of any one or more of the foregoing; (2) the annuity contract is not subject to section 403(a) of the Code; (3) the employee's rights under the contract are nonforfeitable except for failure to pay future premiums; (4) such contract is purchased under a plan which meets the nondiscrimination requirements of paragraph (12), except in the case of a contract purchased by a church; and, (5) in the case of a contract purchased under a plan which provides a salary reduction agreement, the plan meets the requirements of section 401(a)(30).

Section 403(b)(1) of the Code provides further that the employee shall include in his gross income the amounts actually distributed under such contract in the year distributed as provided in section 72 of the Code.

Section 403(b)(10) of the Code requires that arrangements pursuant to section 403(b) must satisfy requirements similar to the requirements of section 401(a)(9) and similar to the incidental death benefit requirements of section 401(a) with respect to benefits accruing after December 31, 1986, in taxable years ending after such date. In addition, this section requires that, for distributions made after December 31, 1992, the requirements of section 401(a)(31), regarding direct rollovers, must be met.

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Section 401(a)(9) of the Code, generally, provides that benefits commence by April 1 of the calendar year following the later of the calendar year in which the employee attains age 70½, or the calendar year in which the employee retires, and specifies required minimum distribution rules for the payment of benefits from retirement plans.

Section 403(b)(11) of the Code provides, generally, that section 403(b) annuity contract distributions attributable to contributions made pursuant to a salary reduction agreement (within the meaning of section 402(g)(3)(C)) may be paid only when the employee attains age 59½, separates from service, dies, becomes disabled (within the meaning of section 72(m)(7)), or in the case of hardship. Such contract may not provide for the distribution of any income attributable to such contributions in the case of hardship.

Section 403(b)(1)(E) of the Code provides that in the case of a contract purchased under a plan which provides a salary reduction agreement, the plan must meet the requirements of section 401(a)(30). Section 401(a)(30) requires a section 403(b) arrangement, which provides for elective deferrals, to limit such deferrals under the arrangement, in combination with any other qualified plans or arrangements, of an employer maintaining such plan, providing for elective deferrals, to the limitation in effect under section 402(g)(1) for taxable years beginning in such calendar year.

Section 402(g)(1) of the Code provides, generally, that the elective deferrals of any individual for any taxable year shall be included in such individual's gross income to the extent the amount of such deferrals exceeds $7,000.

Section 402(g)(3)(C) provides that the term "elective deferrals" includes, in part, with respect to any taxable year, any employer contribution to purchase an annuity contract under section 403(b) under a salary reduction agreement.

Section 402(g)(3)(D) provides that an employer contribution shall not be treated as an elective deferral described in subparagraph (C) if under the salary reduction agreement such contribution is made pursuant to a one-time irrevocable election made by the employee at the time of initial eligibility to participate in the agreement or is made pursuant to a similar arrangement involving a one-time irrevocable election specified in regulations.

Section 402(g)(4) of the Code provides that the limitation under paragraph (1) shall be increased (but not to an amount in excess of $9,500 ($10,000 for years after December 31, 1997)) by the amount of any employer contributions for the taxable year described in section 402(g)(3)(C).

Section 415(a)(2) of the Code provides, in relevant part, that an annuity contract described in section 403(b) shall not be considered described in section 403(b), unless it satisfies the section 415 limitations. In the case of an annuity contract described in section 403(b), the preceding sentence applies only to the portion of the annuity contract exceeding the section 415 limitations and the amount of the contribution for such portion shall reduce the exclusion allowance as provided in section 403(b)(2).

In this case, you represent that Employer M, an employer described in section 501(c)(3) of the Code, has established Plan X as its section 403(b) program for its employees. All contributions and the earnings thereon are fully vested and nonforfeitable at all times. Plan X does not meet the requirements of a section 403(a) annuity contract.

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Plan X satisfies the limits, under section 403(b)(11) of the Code, that amounts attributable to elective deferrals shall not be distributable earlier than upon the attainment of age 59½ , separation from service, death, disability, or hardship. In addition, Plan X satisfies the section 403(b)(10) requirements and limits contributions in accordance with sections 403(b)(2) and 415 of the Code.

Pre-tax contributions required to be made as a condition of employment are not considered elective deferrals for purposes of section 402(g).

In this case, Plan X provides that participants are required to make these required contributions through a salary reduction agreement, as a condition of employment.

Based on the foregoing law and facts as represented, we conclude that Plan X does satisfy the requirements of section 403(b). As a result of the qualification of Plan X as a section 403(b) arrangement, we rule that an employee who is a participant in Plan X may exclude from gross income amounts contributed in that taxable year, pursuant to the terms of Plan X, which do not exceed the applicable limitations under sections 402(g), 403(b)(2) and 415 of the Code. Furthermore, we rule that distributions from Plan X will be taxed under sections 72 and 403(b)(1). With respect to ruling request number four, pursuant to section 402(g)(3)(D), we rule that pre-tax contributions required to be made as a condition of employment are not "elective deferrals" and, therefore, are not subject to the section 402(g) limit.

This ruling is limited to the form of Plan X as amended, excluding any form defects that may violate the nondiscrimination requirements of section 403(b)(12) of the Code. This ruling does not extend to any operational violations of section 403(b) by Plan X, now or in the future.

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

A copy of this letter has been sent to your authorized representative in accordance with a power of attorney on file in this office.

Sincerely yours, John G. Riddle, Jr., Chief, Employee Plans, Technical Branch 4

John G. Riddle, Jr.