

**Internal Revenue Service
memorandum**

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to: Carol Gold, Director
Employee Plans Division

from: Marjorie Hoffman
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Employee Benefits and Exempt Organizations

subject: Annual Additions under Section 415

We are responding to your request to our office for advice on the issue stated below.

ISSUE

Whether employer contributions are considered annual additions under § 415(c) of the Internal Revenue Code ("Code") for a limitation year in which the contributions are allocated to a participant's account if the contributions remain forfeitable during that year under the plan's vesting schedule which satisfies the requirements of § 411 of the Code.

CONCLUSION

For purposes of determining the maximum contribution limitations under § 415(c) of the Code, unvested employer contributions are considered annual additions for the limitation year in which the contributions were allocated to the account of a plan participant.

DISCUSSION

Statement of Law.

Section 415(a) of the Code provides that in order for a trust, which is part of a pension, profit-sharing, or stock bonus plan, to meet the qualification requirements of § 401(a), the plan must provide benefits within the limitation requirements of § 415. Section 415(c) of the Code provides that the maximum amount that may be allocated to a participant's account in a defined contribution plan cannot exceed the lesser of \$30,000 or 25% of the participant's compensation.

For purposes of applying the § 415(c) limitations, all annual additions allocated to a participant's account for a limitation year are taken into account. Section 415(c)(2) of the

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Code defines annual additions as the sum of employer contributions, employee contributions, and forfeitures for any year. Section 1.415-6(b)(1)(i) of the Income Tax Regulations ("Regulations") elaborates on the statutory definition of annual additions by providing that the above-listed contributions must be credited to participants' accounts during the limitation year in order to be considered annual additions for that time period. Annual additions also include § 401(h) medical account allocations and post-retirement benefits provided to key employees that are allocated to a separate account in accordance with § 419A(d)(1) of the Code.

Section 1.415-2(b)(1) of the Regulations states that the relevant period in which the requirements of § 415 will be applied is the limitation year. The limitation year is the calendar year unless another twelve-month period is elected by the plan sponsor. Section 1.415-6(b)(7) of the Regulations explains that an annual addition is treated as credited to a participant's account for a limitation year if it is allocated to that participant's account under the terms of the plan as of any date within the limitation year.

Section 411 of the Code sets forth the minimum vesting standards, which specify when a participant's right to his or her accrued benefits must become nonforfeitable. Section 411(a)(7)(A)(ii) of the Code defines the accrued benefit of a participant in a defined contribution plan as the balance in his or her account. Section 411(a)(1) of the Code provides that a participant's right to his or her accrued benefit derived from employee contributions is 100% nonforfeitable. In order to satisfy the requirements of § 411 of the Code with respect to employer-provided benefits, the plan must provide that these benefits become nonforfeitable with a vesting schedule that satisfies § 411(a)(2) -- either the five-year cliff vesting described in § 411(a)(2)(A) or the seven-year graded vesting described in § 411(a)(2)(B). However, a plan may always provide a more rapid vesting schedule than is required by § 411 of the Code.

Analysis.

The requirements under §§ 411(a) and 415 of the Code are independent requirements that must be satisfied separately with respect to all retirement benefits provided under a plan for each plan year in order for the plan to remain qualified under § 401(a). Section 411 of the Code provides the rules for when a participant must attain a nonforfeitable right to part or all of his or her accrued benefit. Section 415(c) of the Code imposes limits on the amount that is permitted to be allocated to each participant's account under a defined contribution plan for a limitation year. The extent to which allocations made to any participant's account for a limitation year are nonforfeitable is

irrelevant in determining whether the total amount of the allocations for the limitation year exceeds the limitation requirements of § 415(c)(1) of the Code.

For purposes of applying the § 415(c) limitations for a limitation year, it is necessary to identify annual additions that are allocated as of a date within the limitation year to each participant's account. In general, section 1.415-6(b)(2) of the Regulations provides that contributions made by an employer and allocated to participants' accounts are annual additions. An annual addition shall be deemed credited to a participant's account for a limitation year if it is allocated to his or her account under the terms of the plan as of any date within the limitation year. Thus, in order for employer contributions to be considered annual additions as defined in § 415(c)(2) of the Code, they must be allocated to participants' accounts and those allocations must occur within the plan's limitation year. Employer contributions and forfeitures that are forfeitable as of the date allocated but otherwise satisfy the requirements of § 1.415-6(b) of the Regulations are annual additions for purposes of applying the maximum contribution limitations under § 415 of the Code for the limitation year that contains the allocation date. The character of an allocation as an annual addition under § 415(c) of the Code for the limitation year in which the amount was allocated is not changed merely because the allocation is later forfeited after the employee terminates from employment without sufficient years of service to be vested.

Thus, for purposes of determining the maximum contribution limitations under § 415(c) of the Code, unvested employer contributions are considered annual additions for the limitation year in which the contributions were allocated to the account of a plan participant.


MARJORIE HOFFMAN