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Department of the Treasury  
Washington, DC 20224

Third Party Communication: None  
Date of Communication: Not Applicable

Person To Contact:

Telephone Number:

Refer Reply To:  
CC:TEGE:EB:QP2  
PLR-122391-04

Date:  
October 25, 2004

**Legend**

Employer:

Plan:

Dear \_\_\_\_\_ :

This responds to your letter requesting a ruling concerning the amended and restated Plan which Employer intends to be an eligible deferred compensation plan under section 457(b) of the Internal Revenue Code of 1986 (the Code).

It is represented that Employer is a municipality and an eligible employer within the meaning of section 457(e)(1)(A), and the Plan is intended to be an eligible deferred compensation plan to which section 457(a) applies. Employer initially received a private letter ruling with respect to the Plan on September 27, 1991. The Plan has subsequently been amended, and Employer has received private letter rulings, lastly on February 16, 2001, to the effect that the Plan continues to comply with section 457.

Under the plan an eligible employee becomes a participant by executing an agreement which authorizes Employer to reduce the employee's compensation by a specific amount and to contribute such amount to an account established on behalf of the participant. No portion of the compensation of an employee shall be deferred for any calendar month unless the employee enters into the agreement to do so prior to the beginning of the month. 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 or she attains normal retirement age under the Plan. In

addition, the Plan provides for age 50 plus catch-up contributions described in section 414(v). The amounts that may be deferred under the annual maximum limitation and the catch-up provisions are within the limitations of section 457.

Participants are permitted to choose among various investment options under the Plan for the investment of amounts in their accounts. Subject to the form and manner prescribed by Employer, participants are permitted to change their investment options at their discretion.

With certain limitations, a participant may elect the manner in which his or her deferred amounts will be distributed. The Plan provides that the manner and time of benefit payout must meet the distribution requirements of sections 401(a)(1)(9) and 457(d) of the Code.

The Plan provides that amounts of compensation deferred thereunder are to be transferred to and invested in a custodial account described in sections 457(g)(3) and 401(f) for the exclusive benefit of the participants and their beneficiaries. All amounts deferred under the Plan must be transferred to the custodial account within an administratively reasonable time period, but in no event later than two business days after the applicable payroll date. The rights of any participant or beneficiary to payments pursuant to the Plan are not subject to alienation, transfer, assignment, pledge, attachment, or encumbrance of any kind.

We note that the Internal Revenue Service recently published Revenue Procedure 2004-56, 2004-35 I.R.B. 376, (Aug 10, 2004). Rev. Proc. 2004-56, contains model amendments (the Model Amendment) designed for use by eligible governmental employers maintaining eligible section 457(b) defined contribution plans that permit employees to elect to defer compensation, that are maintained on the basis of the calendar year, and that provide for the use of one or more trusts to satisfy the requirements of section 457(g) of the Code. If an eligible governmental employer adopts one or more of the Model Amendments for its plan that is intended to be an eligible section 457(b) governmental plan, the plan will be treated as meeting the plan requirements for eligibility under section 457(b) with respect to those provisions.

The Plan has been amended to increase the amount of eligible annual deferrals in response to changes in the Code and also adopts several Model Amendment provisions on a word-for-word basis or in a manner that is substantially similar in all material respects.

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)(1)(A) of the Code provides that in the case of a participant in an eligible governmental 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 to the participant or beneficiary.

Section 457(b)(2) limits the amount of eligible annual deferrals. However, a catch-up amount described in section 457(b)(3) may be added to this amount for participants that are within three years of the normal retirement age or, for participants age 50 or older, a catch-up amount may be added as described in section 457(e)(18). The total eligible-deferral amount under these provisions is limited by section 457(c), and the coordination of these provisions is described in Income Tax Regulation § 1.457-4(c).

Section 457(b)(5) prescribes that an eligible deferred compensation plan must meet the distribution requirements of section 457(d). Section 457(d)(1)(A) of the Code 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 1/2, (ii) when the participant has a severance from employment with the employer, or (iii) when the participant is faced with an unforeseeable emergency. Section 457(d)(2) of the Code requires a plan to meet the minimum distribution requirements of section 401(a)(9). However, a governmental plan will not fail to meet the requirements of section 401(a)(9) if it provides for in-service distributions of a limited-dollar amount which meet the requirements of section 457(e)(9)(A) and Income Tax Regulation section 1.457-6(e).

Income Tax Regulation section 1.457-6(e) is satisfied if the participant's total amount deferred (the participant's total account balance) which is not attributable to rollover contributions is not in excess of the dollar limit under section 411(a)(11)(A) (i.e., \$5000 adjusted for inflation), no amount has been deferred under the plan by or for the participant during the two-year period ending on the date of the distribution, and there has been no prior distribution under the plan to the participant of this kind.

Section 457(g) of the Code 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. Section 457(g)(2)(A) provides that a trust described in section 457(g)(1) shall be treated as an organization exempt from tax under section 501(a). Section 457(g)(3) states that custodial accounts and contracts described in section 401(f) of the Code shall be treated as trusts under rules similar to the rules under section 401(f).

Based upon the information submitted and the representations made, we conclude as follows:

1. The amended and restated Plan established by Employer is an eligible deferred compensation plan as defined in section 457(b) of the Code.

2. Amounts of compensation deferred in accordance with the Plan, including any income attributable to the deferred compensation, will be includible under section 457(a)(1)(A) of the Code in the recipient's gross income for the taxable year or years in which amounts are paid to a participant or beneficiary in accordance with the terms of the Plan.

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. If the Plan is significantly modified, this ruling will no necessarily remain applicable.

No opinion is expressed concerning the timing of the inclusion in income of amounts deferred under any deferred compensation plan other than the Plan described above. In addition, this ruling applies only to deferrals made after the date of this ruling.

This ruling is directed only to the Employer and the participants in the Plan submitted by transmittal letter dated February 20, 2004, as revised by amendments submitted on October 18, 2004. Section 6110(k)(3) of the Code 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 your authorized representative.

Sincerely yours,

Robert D. Patchell  
Chief, Qualified Plans Branch 2  
Office of the Division Counsel/  
Associate Chief Counsel  
(Tax Exempt & Government Entities)

cc: