INTERNAL REVENUE SERVICE

Significant Index No: 403.00-00

200116052

********** **********
********** **********
********** (202) 283-****

T:EP:RA:**
JAN 24 2001

Attn: ********** **********

Re: **********

Legend:

State A = **********
County B = **********
Company M = ********** **********
Organization N = **********
Organization 0 = ********** **********
Organization P = **********
Organization Q = **********
Organization R = **********
Plan X = **********
Plan Y = ********** **********
Plan Z = ********** **********

Dear **********

This is in response to your letter dated October 12, 1999, as supplemented by correspondence dated September 14, 2000, November 27, 2000, and January 9, 2001, which was submitted by your authorized representative on your behalf, with respect to the applicability of section 403(b) of the Internal Revenue Code to Plan X.

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

Organization N is exempt from taxation under section 501(c) (3) of the Code, as are its members, Organization 0

253

and Organization P. Organization P is also an entity that is an agency of a political subdivision of County B in State A. Organization 0 and Organization P transferred personal property to Organization N, after which Organization N leased real property from Organizations 0 and P. All employees from Organization 0 and certain employees from Organization P became employees of Organization N.

Prior to the transfer, Organization 0 employees were participants in Plan Y, a plan described under section 403(b) of the Code. Plan Y provided for matching contributions and seven-year graded vesting for such contributions. Effective July 1, 1998, Organization N established Plan X to provide, retirement benefits to it employees. Plan X operates on a calendar year basis.

Plan X provides for a salary reduction agreement under which each employee may agree to a reduction in salary by either a percentage of pay or a dollar amount. The agreement provides that only compensation earned after the effective date of the agreement shall be taken into consideration. The agreement provides that the frequency with which the agreement may be entered into or amended and the ability to revoke such agreement shall be determined under the rules applicable to qualified cash or deferred arrangements. The agreement shall continue indefinitely until amended or terminated by either party (subject to certain conditions) by giving at least thirty days written notice prior to the date of such amendment or termination (i.e., irrevocable with respect to compensation earned while the agreement is in effect).

Section 2.1 of Plan X provides that each employee of Organization N is eligible to participate in the Plan on July 1, 1998, if employed on that date, and if not employed on such date the date of their employment. Section 1.16 of Plan X defines an employee as any individual employed by the employer as a common law employee with the exception of independent contractors and leased employees as described under section 414(n) of the Code.

Section 1.17 of Plan X defines "employer" as organization N and any other organization which (1) is a member of the same controlled group of organizations as

252

200116052

****

Organization N, as determined pursuant to sections 414(b), (c), (m) and (o) of the Code, (2) is a non-profit organization within the meaning of section 501(c) (3) of the Code, (3) is one that Organization N's Board of Directors has authorized to participate, and (4) is an entity that takes appropriate action to adopt the Plan and become a signatory to an annuity contract and/or custodial agreement. In addition, section 1.17 of Plan X defines "employer" to include Organization Q and Organization R, both of which are described under section 501(c) (3) of the Code and are support organizations of Organization N.

Section 3.01(a) of Plan X permits participants to elect by entering into a salary reduction agreement to have elective contributions made to the Plan on their behalf. Section 1.15 of Plan X defines elective contributions as contributions made by the employer pursuant to section 3.01(a) of the Plan which meet the requirements of sections 402(g) and 403(b) of the Code.

Section 4.01(b) of Plan X provides that the amount of elective contributions for any taxable year under the Plan and all other plans of Organization N shall not exceed the dollar limit in effect at the beginning of such taxable year under section 402(g) of the Code. In the event a participant has excess elective contributions, section 4.01(b) of Plan X requires that excess elective contributions, adjusted to reflect any credited investment experience up to the date of distribution, will be distributed no later than April 15 to any participant who designates elective contributions as excess elective contributions for such taxable year.

Section 4.01(c) of Plan X provides that elective contributions are also subject to the exclusion allowance limitations contained in section 403(b) (2) of the Code. Section 4.01(a) of Plan X provides that the total annual additions (as defined in section 415(c) (2) of the Code) made on behalf of the participant for any year will not exceed the limits imposed by section 415 of the Code.

Sections 5.01 of Plan X provides that elective contributions made under the Plan are nonforfeitable at all times. Plan X received transfers attributable to former employees of Organization 0 who were covered by Plan Y and

255

200116052

****

who become employees of Organization N. Plan Y provided matching contributions and seven-year graded vesting for such contributions. Section 1.21 defines the matching account as the portion of a participant's account established on behalf of an employee to hold the amount of employer contributions under Plan Y and the proportionate share of adjustment to market value attributable to the matching account. Section 5.01 of Plan X continues the seven year graded vesting for matching contributions under Plan Y that are transferred to Plan X. Employer contributions made with respect to elective contributions attributable to a participant's service on and after July 1, 1998 shall be maintained in Plan Z, a plan which is intended to satisfy the requirements of sections 401(a) and 401(k) of the Code and which is maintained by Organization N.

Section 7.02 of Plan X provides that funding will be through mutual fund shares held by a custodian or annuity contracts issued by an insurance company. Section 8.02 provides that the mutual funds held by the custodian and/or annuity contracts issued by an insurance company acquired pursuant to Plan X must conform with the provisions of the Plan as well as providing investments that conform to section 403(b) of the Code and the regulations issued thereunder.

Section 2.03 of Plan X provides that participants may designate which annuity contracts or which investment vehicles they choose to invest in. Currently, in excess of ninety-nine and nine-tenths per cent of the participants in Plan X enter into individual annuity contracts with Company M. The remaining less than one-tenth of one per cent of the participants enter into individual custodial agreements with Company M.

Under section 6.03 of Plan X, Organization N may permit participants to borrow amounts from their plan assets provided that the terms and conditions of the loans are consistent with the annuity contract/custodial agreement, section 72 of the Code, and section 7.03 of Plan Z.

Under section 6.01 of Plan X, upon the occurrence of a financial hardship, a participant may make an application

256

****

to withdraw all or part of the value of his account attributable to elective contributions. (but not earnings on such elective contributions) and amounts held in the rollover account. Section 6.01 of Plan X provides a procedure for determining the existence of an immediate and heavy financial need (i.e., a financial hardship) and that a distribution is necessary to satisfy an immediate and heavy financial need.

Section 6.02 of Plan X provides for an in-service distribution option, with respect to participant's account balances as of June 30, 1998, for participants who have attained age fifty-nine and one-half.

Section 4.02 of Plan X provides that amounts attributable to elective contributions are distributed to the participant or the participant's beneficiary after retirement, death, attainment of age fifty-nine and one-half, termination of employment, or financial hardship. In addition, section 5.02 of Plan X provides for the distribution of benefits upon the occurrence of total and permanent disability. Benefits are distributable in accordance with the payout options in the annuity contract and/or custodial agreement.

Section 5.03 of Plan X provides that the distribution provisions of the Plan shall be interpreted and applied in accordance with the requirements of section 401(a)(9) of the code and incorporates such requirements by reference into the Plan.

Under section 3.02 of Plan X, rollover assets may be contributed or transferred directly to the Plan if such amounts are a qualifying distribution, determined pursuant to section 403(b)(8) of the Code and such rollover is within sixty days of the date the assets were distributed to the employee. In addition, the Plan will accept rollovers from qualifying conduit individual retirement arrangements. Rollovers will be credited to an account established on behalf of the employee. Section 5.04 of Plan X provides that a participant eligible for a distribution under the Plan may elect to have any portion of his account balance rolled over directly to a section 403(b) tax-sheltered annuity plan or an individual retirement arrangement described under section 408 of the

Code.

Section 11.04 of Plan X provides that none of the benefits under the Plan shall be subject to the claim of any creditor of the participant or beneficiary and neither the participant nor the beneficiary shall have any right to alienate, commute, anticipate or assign any of the benefits under the Plan. Notwithstanding the provisions of section 11.04 of Plan X, section 11.05 of the Plan provides the benefits provided to the participant are subject to the rights afforded to an alternate payee under a qualified domestic relations order under section 414(p) of the Code. Section 7.01 of Plan X provides that contributions under the Plan may be used only for the exclusive benefit of participants and their beneficiaries.

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

1. Elective deferral contributions to Plan X shall be treated under section 403(b) of the Code as amounts contributed by Organization N; and,
2. Elective deferral contributions to Plan X (and earnings thereon) shall not be taxable in the year contributed, to the extent that such contributions satisfy the applicable limits under sections 402(g)(1), 403(b)(2) and 415 of the Code, but instead will be taxable under section 72 of the Code in the year in which such amounts are received by the participant.

With respect to ruling request one, 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 a 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 contract 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) of the Code must satisfy requirements similar to the 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 provides that, for distributions made after December 31, 1992, the requirements of section 401(a)(31) regarding direct rollovers are met.

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 70 1/2, 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 59 1/2, separates from service, dies, becomes disabled (within the meaning of section 72(m)(7)), or 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 contract 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)(4) of the Code provides that the limitation under paragraph (1) shall be increased (but not to an amount in excess of $9,500 ($10,500 for taxable years after December 31, 1999)) by the amount of any employer contributions for the taxable year described in section 402(g)(3)(C).

Section 402(g)(3) of the Code 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 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 limits. 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 Organization N, 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 requirement of a section 403(a) annuity contract.

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 59 1/2, 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.

Accordingly, based on the foregoing law and facts, we conclude with respect to ruling request one that elective deferral contributions to Plan X shall be treated under section 403(b) of the Code as amounts contributed by Organization N. Further, we conclude with respect to ruling request two that elective deferral contributions to Plan X (and earnings thereon) shall not be taxable in the year contributed, to the extent that such contributions satisfy the applicable limits under sections 402(g)(1), 403(b)(2) and 415 of the Code, but instead will be taxable under section 72 of the Code in the year in which such amounts are received by the participant.

This ruling is contingent upon the adoption of the amendments to Plan X, as stipulated in your correspondence dated September 14, 2000, November 27, 2000 and January 9, 2001, and will have no effect unless such proposed amendments are adopted.

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 Code provides that it may not be used or cited by others as precedent.

********** 200116052

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,

(signed) JOYCE E. FLOYD

Joyce E. Floyd, Manager
Employee Plans Technical Group 2
Tax Exempt and Government
Entities Division

Enclosures:
Deleted Copy of this Letter
Notice of Intention to Disclose