200315038

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

JAN 15 2003

6IN: 414.07-00
420.00-00

T:EP:RA:T:A1

In Re:

Act =

State A =

County B =

Dear

This is in response to your request for a ruling that the establishment of a section 401(h) account within the Plan and the transfer of excess pension assets to such account in accordance with section 420 of the Internal Revenue Code ("the Code") will not cause the Plan to fail to be a qualified plan under section 401(a) of the Code.

Facts

The Plan was established in 1942 by the County and is a single-employer contributory defined benefit pension plan. Plan benefits and obligations are under authority of the Act. You have represented that the Plan is a governmental plan within the meaning of section 414(d) of the Code. You requested this ruling because the Plan, as a governmental plan, is not subject to the provisions of section 412 of the Code, subsections of which are included by reference in the provisions of section 420 of the Code.

The provisions of the Act apply to each county in the State of A in which a retirement system has been established. The Act provides that each retirement system, when established, shall be administered by a county retirement board. The Act also creates in each county in which a retirement system has been established a county employee's retirement fund consisting of all moneys arising from appropriations made by the county, contributions made by members of the county's retirement system, and all interest earned by investments of moneys of the fund.

Moneys contributed by the county are credited to a county annuity reserve account. Amounts contributed by members are credited to members' annuity reserve accounts.

The Act provides that, upon retirement, members receive a retirement allowance (the "Retirement Allowance") consisting of a member's annuity that is actuarially equivalent to the accumulated contributions in the member's annuity account and a county annuity equal to a (varying) percentage of the member's final salary multiplied by his years of service. The Act also provides that in addition to the Retirement Allowance a county retirement board may grant to retired employees insurance or other similar benefits that the county has granted to other county employees.

On November 30, 2000, the county retirement board of County B (the "Board") passed a resolution that called for a portion of the assets in the county annuity reserve account of the County B employee's retirement fund (the "Fund") to be transferred to a separate medical plan account to be established within the Fund (the "Proposed Transfer"), subject to the receipt of a favorable ruling by the Internal Revenue Service concerning the tax-favored treatment of retirees and current County B employees who make contributions to and receive benefits from the Fund. In accordance with that resolution you request a ruling that the Proposed Transfer will comply with sections 401(h) and 420 of the Code and will not cause the Plan to fail to be a qualified plan.

Law

Section 412(c)(2)(A) of the Code provides that for purposes of that section, the value of the plan's assets shall be determined on the basis of any reasonable actuarial method of valuation which takes into account fair market value used to determine costs under the plan.

Section 412(c)(7)(A) of the Code provides that for purposes of paragraph (6), the term "full funding limitation" means the excess (if any) of -----

(i) the lesser of

(I) the applicable percentage of current liability (including the expected increase in current liability due to benefits accruing during the plan year), or

(II) the accrued liability (including normal cost) under the plan (determined under the entry age normal funding method if such accrued liability can not be directly calculated under the funding method used for the plan), over

(ii) the lesser of

(I) the fair market value of the plan's assets, or

(II) the value of such assets determined under paragraph (2) of that section

Section 412(c)(7)(B) of the Code provides that for purposes of subparagraph (D) and subclause (I) of subparagraph (A)(i), the term "current liability" has the meaning given such term by subsection (l)(7) (without regard to subparagraphs (C) and (D) thereof) and using the rate of interest used under subsection (b)(5)(B).

Section 412(h)(3) of the Code provides that that section shall not apply to any governmental plan (within the meaning of section 414(d)).

Section 420(a)(1) of the Code provides that if there is a qualified transfer of any excess pension assets of a defined benefit plan (other than a multiemployer plan) to a health benefits account which is part of such plan, a trust which is part of such plan shall not be treated as failing to meet the requirements of subsection (a) or (h) of section 401 solely by reason of such transfer (or any other action authorized under that section).

Section 420(e)(2) of the Code provides that the term "excess pension assets" means the excess (if any) of

(A) the amount determined under section 412(c)(7)(A)(ii) over

(B) the greater of

(i) the amount determined under section 412(c)(7)(A)(i), or

(ii) 125 percent of current liability (as defined in section 412(c)(7)(B))

The determination under section 420(e)(2) shall be made as of the most recent valuation date of the plan preceding the qualified transfer.

Analysis

The Plan is a pension plan and thus, subject to the provisions of section 401(h) of the Code, may establish a separate health benefit account within the Plan. The Plan is not a multi-employer plan and thus, subject to the provisions of section 420 of the Code, may transfer assets to such a health benefits account without causing the Plan to be treated as failing to satisfy the requirements of subsections (a) and (h) of section 401(a) of the Code solely by reason of such transfer.

The fact that the Plan is a governmental plan does not bar the Plan from transferring excess pension assets to a separate health benefits account within the meaning of section 420 of the Code. Multiemployer plans are the only type of defined benefit plans expressly excluded by statutory language from making section 420 transfers. However, the general exemption of governmental plans from the requirements of section 412 of the Code (provided in section 412(h)(3)) does not provide an exemption from the technical requirements of certain provisions of section 420 that reference subsections of section 412.

Thus, a governmental plan, in order to comply with the requirements of section 420 of the Code must determine the amount of available excess assets available for transfer in accordance with section 420(e)(2) of the Code, and therefore must make the determinations provided for in sections 412(c)(7)(A)(i), 412(c)(7)(A)(ii), and 412(c)(7)(B) of the Code, notwithstanding the general exclusion of governmental plans from section 412. The fact that a governmental plan might not perform these calculations in the normal course of operations does not alter the fact that the meaning of the term "excess pension assets" for a governmental plan is the amount derived from performing the computations described in section 420(e)(2).

Therefore the transfer of excess pension assets to a retiree health account (satisfying the requirements of section 401(h) of the Code) within a qualified governmental plan is permitted under section 420 of the Code provided that such transfer satisfies the requirements of section 420, including, as noted above, the requirements of section 420 that reference subsections of section 412 of the Code.

Section 6.03 of Revenue Procedure 2002-4, 2002-1 IRB 127, provides that the Employee Plans Technical office ordinarily will not issue letter rulings on matters involving a plan's qualified status under sections 401 through 420 of the Code and section 4975(e)(7) of the Code and that matters involving a plan's qualified status are generally handled by the Employee Plans Determination program as provided in Rev. Proc. 2003-6 of 2003-1 IRB 191, Rev. Proc 93-19, and Rev. Proc. 93-12.

Therefore, we can not rule as to whether the Proposed Transfer in accordance with the Board resolution of November 30, 2000, will cause the Plan to fail to meet the requirements of sections 401(a) of the Code.

This letter is directed only to the taxpayer that 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 is being furnished to your authorized representative pursuant to a power of attorney (Form 2848) on file.

If you have any questions on this letter, please contact

Sincerely,

James E. Holland, Jr., Manager
Employee Plans Technical