Internal Revenue Service

SIN: 414.07-00

Department of the Treasury

Washington, DC 20224

199903052

Person to Contact:

Telephone Number:

Refer Reply to: CP:E:EP:T:2

Date: OCT 30 1998

Legend:

Plan A =

County B =

Unions C =

Board D =

State Committee E =

Dear :

This is in response to a letter dated April 3, 1998, as supplemented by letter dated July 9, 1998, submitted by your authorized representative for a ruling concerning the federal income tax treatment under Internal Revenue Code section §414(h)(2) of certain contributions to Plan A.

Your authorized representative submitted the following facts and representations:

Plan A is maintained by County B. Plan A is a defined benefit plan that is qualified under section 401(a) of the Internal Revenue Code and its related trust is exempt from taxation under section 501(a) of the Code.

Plan A has historically been funded through a combination of County B's contributions and participants' contributions. Participation in the Plan and the payroll deduction for the participant contributions are a term and condition of employment. All participants who meet the eligibility requirement for participation in the Plan must make the member contributions. The only exception to mandatory participation in

Plan A applies to elected officials. These individuals have the option of becoming participants in Plan A or refraining from participation. All participant contributions were contributed by employees on an after-tax basis.

Pursuant to collective bargaining, County B and Unions C have agreed to add a feature to Plan A. As a matter of policy, County B has also determined that this provision should also apply to employees who are not members of any collective bargaining unit. This provision is contained in proposed section 9.2(f) of Plan A and provides that County B will make the contributions on behalf of all members and that no member will have the option of receiving the contribution instead of having it contributed to the pension plan.

Board D will adopt the proposed provision after receipt of a favorable letter ruling. The proposed amendment to Plan B, section 9.02(f), will be effective on the latter of the date (1) State Committee E approves the amendment, (2) the date the application for letter ruling is issued, (3) January 1, 1999, or (4) the date of adoption of the amendment by Board D.

Based on the foregoing facts and representations, your authorized representative has requested the following rulings:

(1) That the provisions of the proposed section 9.02(f) of Plan A satisfy the requirements of §414(h)(2) of the Code.

(2) That no part of County B's contributions to Plan A on behalf of (a) elected officials who elect to participate and to have their contribution picked up and (b) employees other than elected officials, will be includable as gross income for federal income tax purposes in the year of contribution with respect to such employees.

(3) That no part of the contributions of County B which are pick up contributions made by it on behalf of its employees pursuant to the proposed section 9.02(f) will be wages for federal income tax purposes in the taxable year in which they were contributed to Plan A.

Section 414(h)(2) of the Code provides that contributions, otherwise designated as employee contributions, shall be treated as employer contributions if such contributions are made to a plan described in section 401(a) established by a state government or a political subdivision thereof and are picked up by the employing unit.

The federal income tax treatment to be accorded contributions which are picked up by the employer within the meaning of section 414(h)(2) of the Code is specified in Revenue Ruling 77-462, 1977-2 C.B. 358. In that revenue ruling, the employer school district agreed to assume and pay the amounts employees were required by state law to contribute to a state

pension plan. Revenue Ruling 77-462 concluded that the school district's picked-up contributions to the plan are excluded from the employees' income until such time as they are distributed to the employees.

The issue of whether contributions have been picked up by an employer within the meaning of Code section 414(h)(2) is addressed in Revenue Ruling 81-35, 1981-1 C.B. 255 and Revenue Ruling 81-36, 1981-1 C.B. 255. These revenue rulings established that the following two criteria must be met: (1) the employer must specify that the contributions, although designated as employee contributions are being paid by the employer in lieu of contributions by the employee; and (2) the employee must not be given the option of choosing to receive amounts directly instead of having them paid by the employer to the pension plan.

In Revenue Ruling 87-10, 1987-1 C.B. 136, the Internal Revenue Service considered whether contributions designated as employee contributions to a governmental plan are excludable from the gross income of the employee. The Service concluded that to satisfy the criteria set forth in Revenue Rulings 81-35 and 81-36 with respect to particular contributions, the required specification of designated employee contributions must be completed before the period to which such contributions relate.

The proposed amendment to Plan A and the elected officials' Participation Election form satisfy the criteria set forth in Rev. Rul. 81-35 and Rev. Rul. 81-36 by providing that County B will make contributions in lieu of contributions by employees and that employees may not elect to receive such contributions directly.

Accordingly, we conclude as follows:

(1) That the provisions of the proposed section 9.02(f) of Plan A satisfy the requirements of §414(h)(2) of the Code.

(2) That no part of County B's contributions to Plan A on behalf of (a) elected officials who elect to participate and to have their contribution picked up and (b) employees other than elected officials, will be includable as gross income for federal income tax purposes in the year of contribution with respect to such employees.

(3) That no part of the contributions of County B which are pick up contributions made by it on behalf of its employees pursuant to the proposed section 9.02(f) will be wages for federal income tax purposes in the taxable year in which they were contributed to Plan A.

These rulings apply only if the effective date for the commencement of any proposed pick up as specified in the proposed amendment is the later of the items specified in §9.2(f) or the date the pick up is put into effect.

The above ruling is based on the assumption that the plan sponsored by System A will be qualified under section 401(a) of the Code and its related trusts will be tax-exempt under section 501(a) at the time of the proposed contributions.

No opinion is expressed as to whether the amounts in question are subject to tax under the Federal Insurance Contributions Act. No opinion is expressed as to whether the amounts in question are paid pursuant to a "salary reduction agreement" within the meaning of section 3121(v)(1)(B).

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

Sincerely,

(signed) JOYCE E. FLOYD

Joyce E. Floyd
Chief, Employee Plans
Technical Branch 2

Enclosure:

Deleted copy of this ruling
Notice 437

cc: