

[4830-01-p]

DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

[REG-157714-06]

RIN 1545-BG43

Determination of Governmental Plan Status

AGENCY: Internal Revenue Service (IRS), Department of the Treasury.

ACTION: Advance notice of proposed rulemaking.

SUMMARY: The Treasury Department and IRS anticipate issuing regulations under section 414(d) of the Internal Revenue Code (Code) to define the term “governmental plan.” This document describes the rules that the Treasury Department and IRS are considering proposing relating to the determination of whether a plan is a governmental plan within the meaning of section 414(d) and contains an appendix that includes a draft notice of proposed rulemaking on which the Treasury Department and IRS invite comments from the public. This document applies to sponsors of, and participants and beneficiaries in, employee benefit plans that are determined to be governmental plans.

DATES: Written or electronic comments must be received by February 6, 2012.

ADDRESSES: Send submissions relating to the section 414(d) draft general regulations to: CC:PA:LPD:PR (REG-157714-06), room 5203, Internal Revenue Service, PO Box 7604, Ben Franklin Station, Washington DC, 20044. Submissions may be hand delivered Monday through Friday, between the hours of 8 a.m. and 4 p.m. to

CC:PA:LPD:PR (REG-157714-06), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, NW., Washington, DC.

Alternately, taxpayers may submit comments relating to the section 414(d) draft general regulations electronically via the Federal eRulemaking Portal at www.regulations.gov (IRS-REG-157714-06).

FOR FURTHER INFORMATION CONTACT:

Concerning the ANPRM, Pamela R. Kinard, at (202) 622-6060; concerning submission of comments, Richard A. Hurst, at Richard.A.Hurst@irs.counsel.treas.gov or at (202) 622-7180 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

Background

This document describes rules that the Treasury Department and IRS are considering proposing and contains a draft notice of proposed rulemaking (in the Appendix to this ANPRM) under section 414(d) of the Internal Revenue Code (Code). Under the draft notice of proposed rulemaking (in the Appendix to this ANPRM), the rules would provide general guidance relating to the determination of whether a retirement plan is a governmental plan within the meaning of section 414(d) (section 414(d) draft general regulations). The principles described in this ANPRM could also apply for purposes of certain parallel terms in sections 403(b) and 457 of the Code.

Section 414(d) of the Code provides that the term "governmental plan" generally means a plan established and maintained for its employees by the Government of the United States, by the government of any State or political subdivision thereof, or by any agency or instrumentality of any of the foregoing. See sections 3(32) and 4021(b)(2) of

the Employee Retirement Income Security Act of 1974 (ERISA) for definitions of the term “governmental plan,” which govern respectively for purposes of title I and title IV of ERISA¹.

The term “governmental plan” also includes any plan to which the Railroad Retirement Act of 1935 or 1937 (49 Stat. 967, as amended by 50 Stat. 307) applies and which is financed by contributions required under that Act and any plan of an international organization which is exempt from taxation by reason of the International Organizations Immunities Act (59 Stat. 669). See section 414(d)(2) of the Code.

Section 414(d) was amended by the Pension Protection Act of 2006, Public Law 109-280 (120 Stat. 780) (PPA '06) to include certain plans of Indian tribal governments and related entities.² Section 906(a)(1) of PPA '06 provides that the term “governmental plan” includes a plan which is established and maintained by an Indian tribal government (as defined in section 7701(a)(40)), a subdivision of an Indian tribal government (determined in accordance with section 7871(d)), or an agency or instrumentality of either (ITG), and all the participants of which are employees of such entity substantially all of whose services as such an employee are in the performance of essential governmental functions but not in the performance of commercial activities (whether or not an essential governmental function).

Neither section 414(d) of the Code, section 3(32) of ERISA, nor section 4021(b)(2) of ERISA define key terms relating to governmental plans, including the terms “established and maintained,” “political subdivision,” “agency,” and

¹ The three definitions of the term “governmental plan” are essentially the same. The only difference is that, in defining the term “governmental plan,” section 3(32) of ERISA uses the phrase “established or maintained,” whereas section 414(d) of the Code and section 4021(b) of ERISA use the term “established and maintained.”

² Section 906(a) of PPA '06 made similar amendments to sections 3(32) and 4021(b)(2) of ERISA.

“instrumentality.” Currently, there are no regulations interpreting section 414(d). Revenue Ruling 89-49 (1989-1 CB 117), see §601.601(d)(2), sets forth a facts and circumstances analysis for determining whether a retirement plan is a governmental plan within the meaning of section 414(d).³ This analysis is used by the IRS in issuing letter rulings.

Governmental plans are subject to different rules than retirement plans of nongovernmental employers. Governmental plans are excluded from the provisions of titles I and IV of ERISA. In addition, governmental plans receive special treatment under the Code. These plans are exempt from certain qualification requirements and they are deemed to satisfy certain other qualification requirements under certain conditions. As a result, the principal qualification requirements for a tax-qualified governmental plan⁴ are that the plan--

- Be established and maintained by the employer for the exclusive benefit of the employer’s employees or their beneficiaries;
- Provide definitely determinable benefits;
- Be operated pursuant to its terms;
- Satisfy the direct rollover rules of section 401(a)(31);
- Satisfy the section 401(a)(17) limitation on compensation;

³ See also Rev. Rul. 57-128 (1957-1 CB 311), see § 601.601(d)(2), which provides guidance on determining when an entity is a governmental instrumentality for purposes of the exemption from employment taxes under section 3121(b)(7) and 3306(c)(7).

⁴ A special rule applies to contributory plans of certain governmental entities. Section 414(h)(2) provides that, for a qualified plan established by a State government or political subdivision thereof, or by any agency or instrumentality of the foregoing, where the contributions of the governmental employer are designated as employee contributions under section 414(h)(1) but the governmental employer picks up the contributions, the contributions picked up will be treated as employer contributions.

- Comply with the statutory minimum required distribution rules under section 401(a)(9);
- Satisfy the pre-ERISA vesting requirements under section 411(e)(2);⁵
- Satisfy the section 415 limitations on benefits, as applicable to governmental plans; and
- Satisfy the prohibited transaction rules in section 503.

State and local governments, political subdivisions thereof, and agencies or instrumentalities thereof are generally not permitted to offer cash or deferred arrangements under section 401(k). However, an ITG is permitted to offer a cash or deferred arrangement under section 401(k).

For further background, see the “Background” section of the preamble in the section 414(d) draft general regulations in the Appendix to this ANPRM under the headings, “Exclusion of Governmental Plans from ERISA,” “Exemption of Governmental Plans from Certain Qualified Plan Rules,” and “Exemption of Governmental Plans from Other Employee Benefit Rules Relating to Retirement Plans.”

Over the past several years, the IRS has been coordinating with the Department of Labor (DOL) and Pension Benefit Guaranty Corporation (PBGC) (the “Agencies”) on governmental plan determinations. Although the anticipated proposed regulations would only be applicable for purposes of section 414(d), the DOL and PBGC were consulted when drafting this proposal. DOL and PBGC agreed that it would be advantageous for the Agencies and the regulated community for there to be coordinated criteria for determining whether a plan is a governmental plan within the meaning of

⁵ Section 411(e)(2) states that a plan described in section 411(e)(1) is treated as meeting the requirements of section 411 if the plan meets the vesting requirements resulting from the application of section 401(a)(4) and (a)(7) as in effect on September 1, 1974.

section 414(d) of the Code, section 3(32) of ERISA, and section 4021(b)(2) of ERISA. See the “Background” section of the preamble in the section 414(d) draft general regulations in the Appendix to this ANPRM under the heading, “Interagency Coordination on Governmental Plan Determinations.”

The Treasury Department and the IRS have determined to seek public comment on the draft proposed regulations in the Appendix to this ANPRM in advance of issuing a notice of proposed rulemaking. In light of the interaction of the governmental plan definitions in the Code and ERISA, a copy of the comments will be forwarded to DOL and PBGC.

Explanation of Provisions

Attached to the Appendix to this ANPRM is a draft notice of proposed rulemaking. The draft regulations include proposed rules, a preamble, and a request for comments. The Treasury Department and IRS invite the public to comment on the rules that the Treasury Department and IRS are considering proposing, which would generally define the term “governmental plan” within the meaning of section 414(d), as well as other key related terms, including “State,” “political subdivision of a State,” and “agency or instrumentality of a State or political subdivision of a State.”

In determining whether an entity is an agency or instrumentality of the United States or an agency of instrumentality of a State or political subdivision of a State, the anticipated guidance would provide a facts and circumstances analysis. The factors used in these analyses are drawn from the factors historically used in governmental plan determinations, including Rev. Ruls. 57-128 and 89-49. The anticipated guidance would provide several examples illustrating the application of the facts and

circumstances tests. See the “Explanation of Provisions” section in the section 414(d) draft general regulations in the Appendix to this ANPRM under the headings, “Definitions of the United States and agency or instrumentality of the United States” and “Definition of agency or instrumentality of a State or a political subdivision of a State.” See §601.601(d)(2).

The anticipated proposed regulations would include numerous factors for determining whether an entity is an agency or instrumentality of a State or a political subdivision of a State. The section 414(d) draft proposed regulations in the Appendix to this ANPRM would categorize these factors into major factors and other factors. The section 414(d) draft general regulations would also request comments from the public on whether the final regulations should eliminate the distinction between main and other factors. In addition, the section 414(d) draft general regulations would request comments on the ordering and application of main and other factors; for example, whether, as an alternative to the ranking of major factors and other factors, the regulations could provide a safe harbor standard focusing on control and fiscal responsibility under which the entity would be treated as an agency or instrumentality of a State or a political subdivision of a State. For further explanation of the safe harbor standard, see the “Comments and Public Hearing” section in the preamble of the section 414(d) draft general regulations, which is located in the Appendix to this ANPRM.

The anticipated proposed regulations do not address the special rules that apply in determining whether a plan of an Indian tribal government is a governmental plan within the meaning of section 414(d). That topic would be reserved in the proposed

regulations and is addressed in an ANPRM (REG-133223-08) that is being published elsewhere in this issue of the **Federal Register**.

The anticipated proposed regulations would provide rules for determining whether a governmental entity has established and maintained a plan for purposes of section 414(d). The anticipated proposed regulations might provide that a plan is established and maintained for the employees of a governmental entity if: (1) the plan is established and maintained by an employer within the meaning of §1.401-1(a)(2), (2) the employer is a governmental entity, and (3) the only participants covered by the plan are employees of that governmental entity. The anticipated proposed regulations might also provide rules covering circumstances involving a change in status of an entity (that is, when a private entity becomes a governmental entity or when a governmental entity becomes a private entity) due to an acquisition or asset transfer. See the “Explanation of Provisions” section in the section 414(d) draft general regulations in the Appendix to this ANPRM under the heading, “Requirements for establishing and maintaining a section 414(d) governmental plan.”

Recognizing that the guidance might affect numerous governmental plan participants and their beneficiaries, the anticipated proposed regulations request comments on transition rules, including transitional relief for governmental plans that permitted participation of a small number of former employees in their plans. See the “Comments and Public Hearing” section in the preamble of the section 414(d) draft general regulations that is located in the Appendix to this ANPRM.

Request for Comments

Before the notice of proposed rulemaking is issued, consideration will be given to any written comments that are submitted timely (preferably a signed original and eight (8) copies) to the IRS. All comments will be available for public inspection and copying. Copies of the comments will be provided to the DOL and PBGC.

The IRS and Department of Treasury plan to schedule a public hearing on the ANPRM. That hearing will be scheduled and announced at a later date. In addition to a public hearing, the Treasury Department and IRS anticipate scheduling “Town Hall” meetings in order to obtain comments from the public on the section 414(d) draft general regulations. It is expected that these “Town Hall” meetings will take place in different locations across the country. Participants will be encouraged to pre-register for the meetings. Information relating to these “Town Hall” meetings, including dates, times, locations, registration, and the procedures for submitting written and oral comments, will be available on the IRS website relating to governmental plans at <http://www.irs.gov/retirement/article/0,,id=181779,00.html>.

Drafting Information

The principal author of this advance notice of proposed rulemaking is Pamela R.

Kinard, Office of the Chief Counsel (Tax-exempt and Government Entities), however, other personnel from the IRS and Treasury Department participated in its development.

Deputy Commissioner for Services and Enforcement.