

GUIDE TO THE PROPOSED 415 REGULATIONS FOR QUALIFIED GOVERNMENTAL PLANS*

Treas. Reg. Section and Heading	Summary of Contents	Commentary
Existing Treas. Reg. § 1.415-1 through § 1.415-10	These existing provisions will be removed upon the adoption of new regulations.	In addition to replacing existing regulations on Code Section 415, the IRS in the preamble to the Proposed Regulations seeks comments on Code Section 415(m) and (n).
Prop. Treas. Reg. § 1.415(a)-1. General rules with respect to limitations on benefits and contributions under qualified plans		
1.415(a)-1(a): Trusts	Compliance with Code Section 415 and Proposed Regulations is required for qualified (401(a)) plans.	
1.415(a)-1(b): Certain annuities and accounts	Compliance with Code Section 415 and Proposed Regulations is required for 403(a) plans, 403(b) plans, and Simple 408(k) plans.	
1.415(a)-1(c): Regulations	Outline of Proposed Regulations.	
1.415(a)-1(d): Plan provisions	Plan provisions must preclude violations of 415 limits, but incorporation by reference is permitted. Special rules are provided for automatic freeze provisions, default provisions, optional provisions, cost-of-living adjustments. This provision of the Proposed Regulations prohibits accruals in excess of 415(b) limits.	<p>Incorporation by reference can be a useful tool for governmental plans, but some state constitutions have been interpreted to limit this drafting option. In addition, incorporation by reference is not feasible where the regulations may be applied in more than one manner and no default is provided.</p> <p>The limitation on benefit accruals will be harmful to governmental plans. <u>See Ice</u></p>

* On May 31, 2005, the IRS issued proposed regulations (REG-130241-04) ("Proposed Regulations") relating to limits on qualified plans under Internal Revenue Code ("Code") Section 415. This guide provides an annotated index of those provisions of the Proposed Regulations that affect qualified governmental plans. The Proposed Regulations may be found at 70 FR 31214-01. Our comments to Treasury and the IRS are attached.

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		Miller Comment Letter, 7/25/2005.
1.415(a)-1(e): Rules for plans maintained by more than one employer	Benefits and contributions attributable to participant from all employers maintaining the plan must be taken into account.	
1.415(a)-1(f): Special rules	This subsection provides rules governing affiliated employers, affiliated service groups, leased employees, permissive service credit under governmental plans, and effect of 415 on other requirements. With regard to QDROs, one 415 limit applies to the total benefit.	In the preamble to the Proposed Regulations, the IRS indicated that regulations do not address Code Section 415(n). However, this subsection of the Proposed Regulations states that 415(n) contains "rules regarding the application of the limitations of sections 415(b) and (c) where an employee makes contributions (including a transfer described in section 403(b)(13) or section 457(e)(17)) to a defined benefit governmental plan to purchase permissive service credit under the plan."
1.415(a)-1(g): Effective date	The general effective date, except as otherwise provided, is limitation years beginning on and after January 1, 2007. A plan in effect before 1/1/07 may apply the Proposed Regulations to limitation years beginning after final regulations are published. A grandfather rule is provided for preexisting benefits (before May 31, 2005) if such plan met statutory provisions, regulations, and other published guidance in effect on May 31, 2005.	Implementation of a new plan after May 31, 2005, but before the final regulations, may present difficulties because of the uncertainty about final regulations and the significant questions that exist under the Proposed Regulations.
Prop. Treas. Reg. § 1.415(b)-1: Limitations for defined benefit plans		
1.415(b)-1(a): General rules	This section provides the general 415(b) limits, the definition of defined benefit plan, a description of required provisions, and adjustments to the dollar limitation of benefit commencement before age 62 and after age 65.	The Proposed Regulations provide that governmental plans are exempt from the Compensation Limit. The Proposed Regulations also provide a cross reference to the TAMRA election under Code Section 415(b)(10). However, no guidance is provided on that election.

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1.415(b)-1(b): Annual benefit	Annual benefit is defined as the "benefit payable annually in the form of a straight life annuity." Any other form of benefit other than qualified joint and survivor annuities (QJSA) must be converted to a straight life annuity for testing purposes. The annual benefit does not include the benefit attributable to after-tax employee contributions or rollover contributions, subject to certain requirements. Picked-up contributions are to be treated as employer contributions to a DB plan for 415 testing purposes. After-tax mandatory and voluntary contributions are treated as contributions to a DC plan. Repaid member contributions meeting certain requirements are not treated as employee contributions, even if paid on an after-tax basis. This section also provides for the determination of annual benefits in the case of multiple annuity starting dates. The final element of this section addresses transferred benefits. This section recognizes that a governmental plan may offer a QEBA, but provides no regulations with regard to the QEBA.	This section poses many challenges for governmental plans. As has been noted in many comments, the multiple annuity starting date provisions will impact many common forms of post-retirement benefit provisions. (See 1.415(b)-2 below.) In addition the Proposed Regulations rely on Code Section 411 and 417 in determining the annual benefit; neither of these sections are applicable to governmental plans. See Ice Miller Comment Letter, 7/25/2005.
1.415(b)-1(c): Adjustments to form of benefit for forms other than a straight life annuity	For a governmental plan, the conversion factors for other forms of benefit are either the plan's factors or 5% interest rate and the applicable mortality table, whichever results in the greater benefit. No adjustment is required for a QJSA or for ancillary benefits. A social security supplement is not considered an ancillary benefit. Consistent with PLR 200452039, the Proposed Regulations provide an example of how a fixed automatic COLA reduces the 415(b) limit.	This section provides more flexibility than prior regulations with regard to the QJSA in that it addresses a situation where a benefit is paid partially as an annuity and partially as a lump sum. However, the fixed COLA provisions could have a detrimental impact. It could significantly increase the number of members who approach the 415(b) limits. See Ice Miller Comment Letter, 7/25/2005.
1.415(b)-1(d): Adjustment to section 415(b)(1)(A) dollar limit for commencement before age 62	The dollar limit is reduced for a benefit commencement before age 62. But governmental plans have an exception for full-time employees of police or fire departments who provide police, firefighting, or emergency medical services. An exception is also provided for survivor and disability benefits.	This provision is very beneficial for public safety governmental plans. However, commentators are seeking additional flexibility for defining public safety employees. See Ice Miller Comment Letter, 7/25/2005.

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1.415(b)-1(e): Adjustment to section 415(b)(1)(A) dollar limit for commencement after age 65	In general, the dollar limit is increased for a benefit commencement after age 65. However, for governmental plans that do not provide actuarial adjustments post-age 65 (which many do not), this increase will not apply.	
1.415(b)-1(f): Total annual payments not in excess of \$10,000	This subsection provides an exception from 415(b) testing for a benefit that does not exceed \$10,000. However, the rule does not apply if the participant has participated in his/her employer's defined contribution plan. For purposes of this subsection, mandatory employee contributions to a defined benefit plan and 401(h) accounts are not considered defined contribution plans.	With the clarifications provided in this section, a governmental plan may wish to consider adding a "screen" for benefits that do not exceed \$10,000/year, so that they are not subjected to 415(b) testing. However, if members of the plan also participate in other 401(a) qualified plans, this would not be an appropriate change to make.
1.415(b)-1(g): Special rule for participation or service of less than 10 years	The dollar limit is reduced pro-rata if a participant has fewer than 10 years of participation in the plan. This reduction is not applicable to a governmental plan distribution of survivor benefits or disability benefits.	

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Prop. Treas. Reg. § 415(b)-2: Multiple annuity starting dates		
1.415(b)-2(a): Determination of annual benefit where distributions have occurred before the current determination date	<p>The annual benefit subject to the Code Section 415(b) limit at a specified determination date, when there are multiple annuity starting dates, is the sum of:</p> <ul style="list-style-type: none"> ▪ The accrued benefit that has not commenced ▪ The annual benefit determined for any distribution with an annuity starting date that occurs within the current limitation year and on or before the current determination date ▪ The annual benefit determined for any remaining amounts payable under a distribution with an annuity starting date that commenced in a prior year ▪ The annual benefit attributable to prior distributions. 	<p>The multiple annuity starting date rules will have a major impact on governmental plans, particularly those that provide ad hoc post-retirement increases, PLSO or DROP benefits, and supplemental or recalculated annuities to reemployed retirees. The most significant impact may be the enormous administrative complexities that some plans will face. Consequently, this is one of the primary respects in which the rules need to be changed. See Ice Miller Comment Letter, 7/25/2005.</p>
1.415(b)-2(b): Annual benefit attributable to prior distributions	<p>The annual benefit attributable to a prior distribution is determined by adjusting that distribution to an actuarially equivalent straight life annuity commencing at the current determination date.</p>	
1.415(b)-2(c): Change in distribution form	<p>If a stream of annuity payments is modified by a new distribution election, the modification is treated as a new annuity starting date.</p>	

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Prop. Treas. Reg. § 1.415(c)-1: Limitations for defined contribution plans		
1.415(c)-1(a): General rules	This section provides the maximum limits on annual additions to a defined contribution plan (401(a), 403(a), and 408(k)). Contributions to the defined contribution portion of a 414(k) plan are subject to these limits, as are non-picked up mandatory and voluntary employee contributions to a defined benefit plan and contributions to an individual medical account under Code Section 401(h).	
1.415(c)-1(b): Annual additions	Annual additions include employer and employee contributions and forfeitures. Exemptions from annual additions include direct transfers between defined contribution plans, restoration of accrued benefits, catch-up contributions, restorative payments, rollovers, repayments of loans.	
1.415(c)-1(c): Examples	This subsection contains examples for 1.415(c)-1(a) and (b).	
1.415(c)-1(e): Special rules for medical benefits	This subsection provides that the 100% of compensation limitation does not apply to an individual medical account under Code Section 401(h).	
Prop. Reg. § 415(c)-2: Compensation		
1.415(c)-2(a): General definition	This subsection establishes the general definition for compensation that is used for 415 purposes.	
1.415(c)-2(b): Items includible as compensation	Compensation includes taxable amounts received by an employee for personal services plus elective deferrals and certain taxable fringe benefits.	It is important to realize that "elective deferrals" are defined specifically as amounts deferred at the employee's election that would be includible in gross income but for the 125 cafeteria plan rules, the 132(f)(4) qualified transportation rules, the 457(b) plan rules, 401(k) plan rules, 403(b) plan rules, and SIMPLE plan rules.
1.415(c)-2(c): Items not includible as compensation	Excluded from compensation are employer contributions to a plan of deferred compensation and distributions from such a plan.	

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1.415(c)-2(d): Safe harbor rules with respect to the plan's definition of compensation	This subsection contains safe harbor definitions that automatically satisfy Code Section 415(c)(3).	
1.415(c)-2(e): Timing rules	Generally, compensation must be paid during the limitation year and prior to severance from employment. However, this subsection provides additional flexibility for certain de minimis timing differences, for certain payments made within 2½ months after severance from employment, and compensation during USERRA service.	This definition of compensation represents a major improvement in the IRS position on the definition of compensation. It allows time to pay out final pay due to the employee, unused sick, vacation and other leave, and bonuses. It does not include actual severance pay for non-qualified deferred compensation. Conforming amendments are made with respect to regulations for 403(b), 457(b), and 401(k) plans. This change is proposed to be effective for limitation years beginning on and after January 1, 2005.
1.415(c)-2(f): Interaction with Section 401(a)(17)	The definition of compensation is subject to 401(a)(17) limits.	This represents a departure from the generally accepted understanding of this issue. However, because governmental plans are not subject to the 100% of compensation limit under Code § 415(b), it has little practical significance for public plans.
1.415(c)-(g): Special rules	This subsection addresses the definition of compensation with respect to employees of a controlled group, permanent and total disability of a defined contribution plan participant, foreign compensation, deemed section 125 compensation, and employees in USERRA Service.	
Prop. Reg. § 1.415(d)-1: Cost-of-living adjustments		
1.415(d)-1(a): Defined benefit plans	This subsection describes the process for increasing the 415(b) limits as prescribed by the IRS.	

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1.415(d)—1(b): Defined contribution plans	This subsection describes the process for increasing the 415(c) limits as prescribed by the IRS.	
1.415(d)-1(d): Implementation of cost-of-living adjustments	A plan is permitted to be amended to reflect these adjustments at any time after the limitations become effective. Or a plan may incorporate the adjustments by reference.	
Prop. Reg. § 1.415(f)-1: Combining and aggregating plans		
1.415(f)-1(a): In general	All defined benefit plans of an employer are treated as one defined benefit plan. All defined contribution plans of an employer are treated as one defined contribution plan.	
1.415(f)-1(b): Affiliated employers, affiliated service groups, and leased employees	Cross reference to applicable rules for plan aggregation for these situations.	
1.415(f)-1(c): Predecessor employer	This subsection provides rules for plan aggregation of former employer that is considered a predecessor employer.	
1.415(f)-1(e): Years of participation and service taken into account when employer maintains more than one defined benefit plan at different times	Years of participation in aggregated plans may be used to meet 10 years-of-service requirement.	
1.415(f)-1(f): Previously unaggregated plans	This subsection provides rules for those situations where previously unaggregated plans are required to be aggregated in a limitation year.	
1.415(f)-1(g): Section 403(b) annuity contracts	In general, a 403(b) annuity contract is not aggregated with a qualified plan maintained by the participant's employer.	
1.415(f)-1(h):	In general, multiemployer plans are not aggregated with other multiemployer plans	

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Multiemployer plans	for purposes of 415 limits.	
1.415(f)-1(j): Special rules for combining certain plans, etc.	This subsection provides rules when a plan, annuity contract, or arrangement is subject to a special limitation and it is combined with a plan that is subject to regular limitations.	
1.415(f)-1(k): Examples	This subsection contains examples of plan aggregation under the Proposed Regulations.	
Prop. Reg. § 1.415(g)-1: Disqualification of plans and trusts		
1.415(g)-1(a): Disqualification of plans	A plan is disqualified for a particular limitation year if for a DC plan annual additions for any participant exceed 415(c) limits and if for a DB plan the annual benefit for any participant exceeds the 415(b) limits.	
1.415(g)-1(b): Rules for disqualification of plans and trusts	Disqualification of the plan is effective as of the first day of first plan year containing any portion of the affected limitation year.	
Prop. Reg. § 1.415(j)-1: Limitation year		
1.415(j)-1(a): In general	Limitation year is the calendar year if no other year is defined.	
1.415(j)-1(b): Alternative limitation year election	The plan may provide for any other consecutive 12-month period as the limitation year.	A plan may only provide for one limitation year regardless of the number or identity of employers maintaining the plan.
1.415(j)-1(c): Multiple limitation years	Where an employer maintains more than one plan, each plan may provide for different limitation years.	
1.415(j)-1(d): Change of limitation year	A limitation year may be changed only by amending plan. Transitional rules are provided for the resulting short limitation period.	

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