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

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TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

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Uniform Issue List: 403.00-00

T:EP:RA:T3

Attention:

Legend:

System A: =

Council B =

Board C =

State M =

Custodian P =

Plan X =

Dear

This is in response to your letter dated January 21, 2001, in which you requested rulings concerning the taxability of contributions made under a plan described in section 403(b) of the Internal Revenue Code. Letters dated March 14, 2001, and April 30, 2002, supplemented the request.

System A is responsible for administering defined contribution retirement plans sponsored by the State M and its political subdivisions. Responsibility for administering these retirement plans has been delegated to the System A by Council B and Board C. Council B is a statutory body responsible for the establishment of qualified retirement plans enacted by the State M Legislature. Board C is a statutory body responsible for the

establishment of nonqualified plans, such as Section 457 plans. System A is an instrumentality of State M.

A number of public technical schools ("Technical Schools") in State M currently sponsor individual tax deferred annuity plans in accordance with the requirements of section 403(b) of the Code. Each of these presently existing 403(b) arrangements has been separately established by the relevant school and is, at present, independently maintained by that school. Each of the technical schools limits participation in its respective 403(b) plan to individuals who are employees of the sponsoring school. Because each of these schools are subagencies of the State M, participation in each plan is open only to individuals described in section 403(b)(1)(A)(ii), and therefore, each arrangement separately satisfies the requirements of section 403(b)(1)(A)

System A , as an instrumentality of the State M, has the authority to administer State M sponsored defined contribution retirement plans.

To achieve consistency, economies of scale and greater efficiency, State M, through the System A proposes to adopt and sponsor Plan X, a section 403(b) tax deferred annuity plan for the employees of the various State M technical schools that currently maintain individual section 403(b) plans. In a private letter ruling issued on May 7, 2002, the Internal Revenue Service determined that Plan X meets the requirements of section 403(b)(1) of the Code. Plan X will be funded with group, fixed and/or variable annuity contracts issued by registered insurance companies and through custodial accounts that hold investments in compliance with the requirements of Section 403(b)(7).

Each individual technical school that currently maintains a separate 403(b) arrangement, as well as other educational institutions in the state whose employees are described in section 403(b)(1)(A)(ii), may elect to become a participating employer under the Plan X.

Among the investment options System A wishes to make available to Plan X participants will be a group annuity and money market option, known as the Fixed Income Option. The fixed income Option will constitute a bundled product consisting of multiple group annuity contracts and the stock of one or more money market registered investment companies to provide added liquidity. The returns on these component instruments will be blended. Each participant will have a divisible interest in each of the underlying investments, and will receive distributions from Plan X at the appropriate time. Each of the underlying investments within the Fixed Income Option will individually meet the investment restrictions place by sections 403(b)(1) and 403(b)(7) of the Code.

The funds will be held by Custodian P, a bank as described in section 408(n) of the Code.

Based on the foregoing, you request a ruling that the Fixed Income Option, which invests exclusively in annuities issued by insurance companies or the stock of one or more regulated investment companies, all pursuant to the requirements of section 403(b)(1) and section 403(b)(7) of the Code, blending of the returns of these underlying investments into the Fixed Income Option will not cause will not cause the Fixed Income Option to fail to meet the requirements of section 403(b)(1).

Section 403(b)(1)(A) of the Code provides 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, 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 an 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, or to a minister described in section 414(e)(5)(A) by the minister or by an employer.

Section 403(b)(7) of the Code states, in part, that amounts paid by an employer described in 403(b)(1)(A) to a custodial account which satisfies the requirements of section 401(f)(2) shall be treated as amounts contributed by him for an annuity contract for the employee if the amounts are to be invested in regulated investment company stock to be held in the custodial account.

Section 401(f)(2) of the Code provides that a custodial account shall be treated as a qualified trust under section 401 if the assets thereof are held by a bank (as defined in section 401(d)(1)) or another person who demonstrates to the satisfaction of the Secretary, that the manner in which he will hold the assets will be consistent with requirements of section 401(a).

Section 1.403(b)-1(h)(3) of the Proposed Income Tax Regulations states that, except as provided in section 403(b)(7)(B) of the Code, a custodial account described in section 403(b)(7) is treated as an annuity contract for all purposes of the Internal Revenue Code.

In this case, Plan X meets the form requirements of section 403(b) of the Code. The Fixed Income Option will consist of both group annuity contracts qualified under section 403(b)(1) of the Code and custodial accounts that meet the requirements of section 403(b)(7). You have represented that each of contributions made pursuant to 403(b)(7), at all times, will only be invested in stock of a regulated investment company and that the contributions made pursuant to 403(b)(1) will be invested only in the group annuity contracts. You have further represented that Custodian P will be purchasing the contract as the custodian of accounts which meet the requirements of section 403(b)(7).

Based on the foregoing, we conclude that the Fixed Income Option, which invests exclusively in annuities issued by insurance companies or the stock of one or more regulated investment companies, all pursuant to the requirements of section 403(b)(1) and section 403(b)(7) of the Code, blending of the returns of these underlying investments into the Fixed Income Option will not cause will not cause the Fixed Income Option to fail to meet the requirements of section 403(b)(1).

This ruling is directed only to the taxpayer who requested it. Section 6110(k)(3) of the Code provides that this ruling may not be used or cited by others as precedent.

Any questions concerning this ruling should be addressed to ********** (ID ***-********) at (***) ***-**** (not a toll free number).

Pursuant to a power of attorney on file in this office, a copy of this letter is being sent to your authorized representative.

Sincerely yours,

Frances V. Sloan

Frances V. Sloan, Manager
Employee Plans Technical Group 3
Tax Exempt and Government Entities Division

Enclosures:
Notice 437
Deleted copy of ruling letter

CC: