

## **Rev. Rul. 2014-24**

### **Investment in group trusts by certain Puerto Rico retirement plans and by certain insurance company separate accounts**

#### **PURPOSE**

This revenue ruling modifies the list of group trust retiree benefit plans eligible to participate in group trusts described in Rev. Rul. 81-100, 1981-1 C.B. 326, as modified by Rev. Rul. 2011-1, 2011-2 I.R.B. 251 (which was modified by Notice 2012-6, 2012-3 I.R.B. 293) (“81-100 group trusts”), to include trusts of certain retirement plans qualified only under the Código de Rentas Internas para un Nuevo Puerto Rico de la Ley Núm. 1 de 31 de enero de 2011 (“Puerto Rico Code”), clarifies that assets held by certain separate accounts maintained by insurance companies may be invested in 81-100 group trusts, and provides limited transition relief.

#### **ISSUES**

1. May a retirement plan that is qualified only under the Puerto Rico Code, and that is described in section 1022(i)(1) of the Employee Retirement Income Security Act of 1974, as amended (“ERISA”) (“section 1022(i)(1) plan”), be a group trust retiree benefit plan eligible to participate in an 81-100 group trust?

2. Under what circumstances may a group trust retiree benefit plan invest in an 81-100 group trust through a separate account maintained by an insurance company without affecting the tax status of either the group trust or the group trust retiree benefit plans participating in the group trust?

## LAW AND ANALYSIS

Rev. Rul. 81-100 provides that qualified retirement plans and individual retirement accounts (IRAs) are permitted to pool their assets for investment purposes in an 81-100 group trust if certain specified requirements are satisfied. Rev. Rul. 2011-1 revised and restated the generally applicable rules for group trusts described in Rev. Rul. 81-100.

Rev. Rul. 2011-1, as modified by Notice 2012-6, permits participation in 81-100 group trusts by certain retiree benefit plans, such as governmental retiree benefit plans under § 401(a)(24), in addition to § 401(a) qualified retirement plans, eligible governmental plan trusts or custodial accounts under § 457(b), annuity contracts under § 403(b), and IRAs, if certain requirements are met. Rev. Rul. 2011-1 collectively refers to the entities permitted to invest in 81-100 group trusts as “group trust retiree benefit plans.”

Rev. Rul. 2011-1 further holds that the tax status of a group trust<sup>1</sup> will be derived from the tax status of the entities participating in the group trust to the extent of the entities’ equitable interests in the group trust if the following requirements are satisfied:

- (1) The group trust is itself adopted as a part of each adopting group trust retiree benefit plan.
- (2) The group trust instrument expressly limits participation to: pension, profit-sharing, and stock bonus trusts or custodial accounts qualifying

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<sup>1</sup> Although tax generally is not imposed on the income of an 81-100 group trust, an 81-100 group trust is liable for any unrelated business income tax that arises under § 511 on account of unrelated business taxable income, as described in § 512, that is generated by the investment of the assets of the group trust. See § 1.511-2(b)(1).

under § 401(a) that are exempt under § 501(a); individual retirement accounts that are exempt under § 408(e); eligible governmental plan trusts or custodial accounts under § 457(b) that are exempt under § 457(g); custodial accounts under § 403(b)(7); retirement income accounts under § 403(b)(9); and § 401(a)(24) governmental plans.

(3) The group trust instrument expressly prohibits any part of its corpus or income that equitably belongs to any adopting group trust retiree benefit plan from being used for, or diverted to, any purpose other than for the exclusive benefit of the participants and the beneficiaries of the group trust retiree benefit plan.

(4) Each group trust retiree benefit plan that adopts the group trust is itself a trust, a custodial account, or a similar entity that is tax-exempt under § 408(e) or § 501(a) (or is treated as tax-exempt under § 501(a)). A group trust retiree benefit plan that is a § 401(a)(24) governmental plan is treated as meeting this requirement if it is not subject to federal income taxation.

(5) Each group trust retiree benefit plan that adopts the group trust expressly provides in its governing document that it is impossible for any part of the corpus or income of the group trust retiree benefit plan to be used for, or diverted to, purposes other than for the exclusive benefit of the plan participants and their beneficiaries.<sup>2</sup>

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<sup>2</sup> In the case of a governmental plan, the governing document includes any statute that sets forth the terms applicable to the plan as well as any regulations, ordinances, and other state or local rules or policies binding on the plan under state or local law.

(6) The group trust instrument expressly limits the assets that may be held by the group trust to assets that are contributed by, or transferred from, a group trust retiree benefit plan to the group trust (and the earnings thereon), and the group trust instrument expressly provides for separate accounting<sup>3</sup> to reflect the interest that each adopting group trust retiree benefit plan has in the group trust, including separate accounting for contributions to the group trust from the adopting plan, disbursements made from the adopting plan's account in the group trust, and investment experience of the group trust allocable to that account. A transaction or accounting method that has the effect of directly or indirectly transferring value from the account of one adopting plan into the account of another adopting plan violates this separate accounting requirement. However, a transaction that merely exchanges investments at fair market value between the accounts of one adopting plan does not violate this separate accounting requirement.

(7) The group trust instrument expressly prohibits an assignment by an adopting group trust retiree benefit plan of any part of its equity or interest in the group trust.

(8) The group trust is created or organized in the United States and is maintained at all times as a domestic trust in the United States.

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<sup>3</sup> Rev. Rul. 2011-1 states that the group trust instrument must provide for separate "accounts" to reflect the interest of each adopting group trust retiree benefit plan. This language has been modified in this revenue ruling to address concerns expressed by commenters that the separate "account" standard could be interpreted more strictly than intended.

### Section 1022(i)(1) Plans

Section 1022(i)(1) of ERISA provides a tax exemption under § 501(a) of the Code for certain plans that satisfy the qualification requirements under the Puerto Rico Code (“section 1022(i)(1) plans”).

In particular, section 1022(i)(1) of ERISA provides that, for purposes of § 501(a), any trust forming part of a pension, profit-sharing, or stock bonus plan all the participants of which are residents of Puerto Rico is treated as an organization described in § 401(a), and therefore generally exempt from income taxation, if the trust both forms part of a pension, profit-sharing, or stock bonus plan and is exempt from income tax under the laws of Puerto Rico. For purposes of section 1022(i) of ERISA, a resident of Puerto Rico is either a bona fide resident of Puerto Rico or a person who performs labor or services primarily within Puerto Rico, regardless of residence for other purposes, and a participant is a current employee who is not excluded under the eligibility provisions of the plan. Section 1.501(a)-1(e). Section 1022(i)(1) of ERISA does not extend qualified status under § 401(a) to a plan, favorable treatment under § 402(a) regarding the taxation of distributions to a participant, or deductions for contributions under § 404(a) to an employer. Section 1022(i)(1) was enacted by Congress in order to provide plans, qualified only under the Puerto Rico Code, with favorable tax treatment with respect to their United States investments to

enable those plans to diversify their investments. H.R. Rep. 93-807 provides the following:

Puerto Rican pension trusts which satisfy the requirements of the Puerto Rican tax law are unable to diversify their portfolio by investing in US securities without paying US income tax on the income derived from such investments since they are not able to qualify for exemption under the US tax law. On the other hand, since the requirements for qualification under US and Puerto Rican law are roughly comparable, a Puerto Rican pension plan is able today to establish a trust in the United States which satisfies both the U.S. and the Puerto Rican tax provisions. Since the Puerto Rican Government has established requirements in its tax law for when a trust forming part of a pension plan for participants who are residents of the Commonwealth of Puerto Rico is entitled to be treated as a qualified trust, your committee believes it is appropriate to eliminate the distinction under US law as to the place of organization or creation of a trust entitled to be qualified under US law, if that trust is created or organized in Puerto Rico and if the trust has satisfied the requirements for qualification under the Puerto Rican tax laws.

Any retirement plan that covers Puerto Rico employees must satisfy the requirements of section 1081.1 of the Puerto Rico Code. The requirements of section 1081.1 of the Puerto Rico Code are similar to the qualification requirements of § 401(a). In particular, section 1081.1(a)(2) of the Puerto Rico Code contains an exclusive benefit requirement similar to the requirement under § 401(a)(2) of the Code.

Furthermore, pursuant to section 3(10) of ERISA, the requirements of Title I of ERISA apply to employee pension benefit plans maintained in Puerto Rico, including section 1022(i)(1) plans. One of those requirements is the exclusive purpose requirement of section 404(a)(1)(A) of ERISA, which provides that a fiduciary shall discharge his duties with respect to a plan solely in the interest of the participants and beneficiaries and for the exclusive purpose of (i) providing benefits to participants and their beneficiaries, and (ii) defraying

reasonable expenses of administering the plan. Section 1081.1(a)(9) of the Puerto Rico Code provides that satisfying the requirements of Title I of ERISA – including the exclusive purpose requirement of section 404(a)(1)(A) of ERISA – is a requirement for maintaining a plan's tax qualified status under the Puerto Rico Code.

The IRS has received inquiries as to whether a section 1022(i)(1) plan may participate in an 81-100 group trust. The inquiries state that sponsors of qualified retirement plans currently participating in 81-100 group trusts want to transfer assets and liabilities to section 1022(i)(1) plans, while continuing to invest the transferred assets in the group trust in order to take advantage of the group trust's broader diversification opportunities and lower investment costs. In response to these inquiries, Rev. Rul. 2011-1 provides in relevant part that the IRS anticipates issuing guidance as to whether a plan described in section 1022(i)(1) of ERISA may participate in an 81-100 group trust and that, until such guidance is issued, the IRS will not treat a group trust as failing to satisfy the requirements of Rev. Rul. 2011-1 merely because the group trust includes the assets of a section 1022(i)(1) plan.

Although a section 1022(i)(1) plan is not a qualified retirement plan under § 401(a) and is not currently listed as a group trust retiree benefit plan under Rev. Rul. 2011-1, it can satisfy the other requirements of Rev. Rul. 2011-1 applicable to group trust retiree benefit plans participating in 81-100 group trusts. Thus, for example, with respect to the requirement of Rev. Rul. 2011-1 that a group trust retiree benefit plan be tax exempt under § 408(e) or § 501(a),

section 1022(i)(1) of ERISA provides that a section 1022(i)(1) trust is tax-exempt under § 501(a).

Also, with respect to the requirement of Rev. Rul. 2011-1 that the governing document of the group trust retiree benefit plan must provide that the assets of the plan must be used for the exclusive benefit of the plan participants and their beneficiaries, a section 1022(i)(1) trust must, pursuant to ERISA and the Puerto Rico Code, be part of a plan that satisfies an exclusive benefit requirement that is very similar to the exclusive benefit rule of § 401(a) and § 1.401(a)-2. Due to this similarity, a section 1022(i)(1) plan that satisfies the exclusive benefit rules of ERISA and the Puerto Rico Code is deemed to satisfy the exclusive benefit requirement of Rev. Rul. 2011-1.

Finally, permitting a section 1022(i)(1) plan to participate in an 81-100 group trust is consistent with the legislative history of section 1022(i)(1) because it permits a 1022(i)(1) plan to diversify its investments without adverse tax consequences to the group trust or its investors.

The remaining standards under Rev. Rul. 2011-1 can be satisfied regardless of whether the participating trust is a section 1022(i)(1) plan or another type of eligible group trust retiree benefit plan.

Accordingly, Rev. Rul. 2011-1 is modified to include section 1022(i)(1) plans on the list of group trust retiree benefit plans eligible to participate in an 81-100 group trust.



### Separate Accounts of Insurance Companies

Rev. Rul. 2011-1 requested comments on whether tax-favored accounts held by plans described in § 401(a) or § 403(b), such as pooled separate accounts supporting annuity contracts that are treated as trusts under § 401(f), should be permitted to invest in 81-100 group trusts. Several comments were received in response recommending that separate accounts maintained by insurance companies should be permitted to invest in 81-100 group trusts if the assets held in such separate accounts were limited to certain types of investors. One commenter suggested that the investors in such separate accounts be limited to group trust retiree benefit plans that are identified in Rev. Rul. 81-100 and any successor rulings. Other commenters recommended that the investors in the separate accounts be limited to qualified retirement plans described in § 401(a) or § 403(a) and/or governmental plans.

The commenters noted that separate accounts<sup>4</sup> maintained by an insurance company are nominally owned by the insurance company but the assets are beneficially owned by the plans invested in the separate accounts and insulated from claims of the company's general creditors under state law. The commenters also noted that assets held in a separate account are not commingled with the assets and liabilities of the company's general account and

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<sup>4</sup> The term "separate account" is not defined for insurance purposes under the Code. For purposes of this revenue ruling, however, it is defined as an account that is segregated from the general asset accounts of the company. This is similar to the definition of a segregated asset account under § 817(d).

are subject to state statutory accounting and reporting requirements as part of the life insurance company's assets.

The federal income tax treatment of the group trust, or of the group trust retiree benefit plans investing in the group trust, does not differ if a plan invests in the group trust through a separate account rather than investing directly in the group trust. The income and gains in a life insurance company separate account that contains only group trust retiree benefit plan assets are not subject to income tax.

Accordingly, in order to clarify the rules pertaining to the investment of separate accounts in group trusts, Rev. Rul. 2011-1 is modified to permit separate accounts to invest in group trusts subject to the conditions set forth in paragraph 2 of the **HOLDINGS** of this revenue ruling.

#### **HOLDINGS**

1. A plan described in section 1022(i)(1) of ERISA is a group trust retiree benefit plan eligible to participate in an 81-100 group trust if the requirements of Rev. Rul. 2011-1, as modified by this revenue ruling, are satisfied.

2. A separate account maintained by an insurance company may invest in an 81-100 group trust without affecting the tax status of either the group trust or the group trust retiree benefit plans participating in the group trust as long as (1) all of the assets in the separate account consist solely of assets of group trust retiree benefit plans as defined in Rev. Rul. 2011-1 and as modified by this revenue ruling, (2) the insurance company maintaining the separate account enters into a written arrangement with the trustee of the group trust consistent

with the requirements of Rev. Rul. 2011-1 (including the requirement that no part of the corpus or income of any of the group trust retiree benefit plans be used for, or diverted to, any purpose other than for the exclusive benefit of the plan participants and their beneficiaries), and (3) the assets of the separate account are insulated from the claims of the insurance company's general creditors.

## **TRANSITION RELIEF**

### Extension of Transfer Relief for Certain Dual-Qualified Plans Participating in Group Trusts

Rev. Rul. 2008-40, 2008-2 C.B. 166, holds that a transfer of assets and liabilities from a qualified retirement plan to a plan that satisfies section 1165<sup>5</sup> of the Puerto Rico Code but is not qualified under § 401(a) is treated as a distribution from the transferor plan, even if the recipient plan is described in section 1022(i)(1) of ERISA. Thus, for example, for a participant who is a bona fide resident of Puerto Rico, the transferred amounts attributable to trust earnings and to employer contributions with respect to services rendered within the United States are treated as income from sources within the United States and, accordingly, are includible in the participant's U.S. income for the taxable year of the transfer. However, Rev. Rul. 2008-40, as modified by Rev. Rul. 2011-1 and Notice 2012-6, also provides that this holding is not effective for a transfer from any qualified retirement plan to a section 1022(i)(1) plan if the date of the transfer is before January 1, 2013.

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<sup>5</sup> Prior to 2011, the requirements applicable to Puerto Rico qualified plans appeared under section 1165 of the Puerto Rico Code and diverged more significantly from the U.S. Internal Revenue Code qualified retirement plan requirements.

A longer period of transition relief is, however, provided with respect to a certain subset of section 1022(i)(1) plans. Specifically, under the heading “Plans Described in Section 1022(i)(1) of ERISA,” Rev. Rul. 2011-1 provides that:

The Service anticipates issuing guidance as to whether a plan described in section 1022(i)(1) of ERISA may participate in an 81-100 group trust. Until such guidance is issued, the Service will not treat a group trust as failing to satisfy the requirements of this revenue ruling merely because the group trust includes the assets of a section 1022(i)(1) plan as long as the section 1022(i)(1) plan (1) was participating in the group trust as of January 10, 2011, or (2) holds assets that had been held by a qualified plan immediately prior to the transfer of those assets to the section 1022(i)(1) plan pursuant to the transition relief in Rev. Rul. 2008-40, as modified by this revenue ruling.

Under Notice 2012-6, the relief provided in paragraphs 2, 3, and 4(b) under the Transition Relief heading in Rev. Rul. 2008-40<sup>6</sup> is extended for transfers to a section 1022(i)(1) transferee plan from a qualified retirement plan that participated in an 81-100 group trust on January 10, 2011, until a deadline to be set forth in future published guidance.

In accordance with Notice 2012-6, this revenue ruling extends the relief provided in paragraphs 2, 3, and 4(b) under the Transition Relief heading in Rev. Rul. 2008-40 to transfers to a section 1022(i)(1) transferee plan from a qualified retirement plan that participated in an 81-100 group trust on January 10, 2011, if the transfer occurs before January 1, 2016. This relief does not apply to

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<sup>6</sup> These paragraphs in Rev. Rul. 2008-40 provide relief (i) from a transfer from a qualified retirement plan to a section 1022(i)(1) plan being treated as a distribution, (ii) relating to the treatment under § 933 of a distribution from a section 1022(i)(1) transferee plan that received a transfer from a qualified retirement plan during the relief period, and (iii) under the § 410(b) minimum coverage rules for a qualified retirement plan that has made a transfer to a section 1022(i)(1) transferee plan.

transfers to section 1022(i)(1) transferee plans from qualified plans that were not invested in group trusts on January 10, 2011.

#### Written Arrangements with Respect to Insurance Company Separate Accounts

In the case of a group trust in which participating group trust retiree benefit plans are invested through an insurance company's separate account as of December 8, 2014, the trustee of the group trust and the insurance company generally are not required to enter into the written arrangement described in paragraph 2 of the **HOLDINGS** before January 1, 2016. In the case of a group trust in which participating retiree benefit plans participate are not invested in the group trust through an insurance company's separate account as of December 8, 2014, but subsequently are invested in the group trust through such a separate account, the trustee of the group trust and the insurance company must enter into such written arrangement no later than the time of the investment.

#### **EFFECT ON OTHER GUIDANCE**

Rev. Rul. 2008-40, Rev. Rul. 2011-1, and Notice 2012-6 are modified.

#### **DRAFTING INFORMATION**

The principal authors of this revenue ruling are Diane Bloom and Robert Walsh of the Employee Plans, Tax Exempt and Government Entities Division. For further information regarding this revenue ruling, please contact the Employee Plans' taxpayer assistance telephone service at 1-877-829-5500 (a toll-free number) between the hours of 8:00 a.m. and 4:30 p.m. Eastern Time, Monday through Friday, or by e-mail at [RetirementPlanQuestions@irs.gov](mailto:RetirementPlanQuestions@irs.gov).