Internal Revenue Service

Department of the Treasury
Washington, DC 20224

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Person To Contact:
, ID No.
Telephone Number:

In Re:

Refer Reply To:
CC:INTL:B01 – PLR-105304-03
Date:
March 16, 2004

TY:

Legend

A =

Country B =
Country C =
Plan =
Employer =
Year 1 =
Year 2 =
Date 3 =
Date 4 =
U.S. City X =
Date 5 =
Date 6 =
Date 7 =
Country D =
Date 8 =
Y =
Z =

Dear :

This is in response to a letter dated December 3, 2002, requesting a ruling with respect to the proper U.S. tax treatment of payments from a domestic pension plan to a nonresident alien individual.

The ruling contained in this letter is based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed

by an appropriate party. While this office has not verified any of the material submitted in support of the request for ruling, it is subject to verification on examination.

FACTS

A is a nonresident alien, and a citizen of Country B, who resides in Country C. A is not a resident of Country B for purposes of the U.S.-Country B income tax treaty. There is no income tax treaty in force between the United States and Country C.

A is entitled to receive a pension under the Plan by reason of his employment by Employer or affiliated companies between Year 1 and Year 2. The trust forming part of the Plan is a trust created or organized in the United States that constitutes a qualified trust under section 401(a) of the Internal Revenue Code. The Plan is a defined benefit plan, meaning it does not provide an individual account for each participant with benefits based solely on the amount of the participant's account. Payments were to begin on or about Date 3 with benefits retroactive to Date 4.

A was employed by Employer in U.S. City X from Date 5 until Date 6. He was rehired on Date 7 to work first in Country D and then in Country C. On or about Date 8, A ceased working for Employer. Thus, A performed Y months of service in the United States and Z months of service outside the United States.

A requests a ruling to determine the portion of each of his pension payments from the Plan that is subject to U.S. federal income tax.

LAW AND ANALYSIS

Section 871(a) of the Code imposes a tax of 30 percent on amounts received by nonresident alien individuals as interest (other than original issue discount as defined in section 1273), dividends, rents, salaries, wages, premiums, annuities, compensations, remunerations, emoluments, and other fixed or determinable annual or periodical gains, profits, and income to the extent the amount so received is from sources within the United States and is not effectively connected with the conduct of a trade or business within the United States.

Section 1441(a) provides, in general, for the withholding of tax at a 30 percent rate on certain income from sources within the United States of nonresident alien individuals.

Section 1441(b) lists salaries, wages, annuities or other fixed or determinable annual or periodical gains as items of income subject to the withholding of tax under section 1441(a).

Section 1.1441-4(b)(1)(ii) of the Income Tax Regulations provides that U.S.-source payments to a nonresident alien individual from a trust described in section 401(a) are subject to withholding under section 1441.

Section 861(a)(3) provides generally that compensation for labor or personal services performed in the United States shall be treated as income from sources within the United States. Section 862(a)(3) provides that compensation for labor or personal services performed outside the United States shall be treated as income from sources without the United States.

Employer contributions to an annuity or pension plan constitute compensation for labor or personal services. See, e.g., Rev. Rul. 56-82, 1956-1 C.B. 59. For purposes of determining the source of pension payments from a retirement plan, the portion of each payment that is attributable to employer contributions with respect to services rendered within the United States is treated as income from sources within the United States, the portion that is attributable to employer contributions with respect to services rendered outside the United States is treated as income from sources without the United States, and the portion that represents earnings and accretions to contributions of either the employer or the employee is treated as income from sources within the United States. Rev. Rul. 79-388, 1979-2 C.B. 270.

Employer contributions to a section 401(a) defined benefit plan covering more than one individual participant are not made for the benefit of specific participants, but are made based on aggregate liabilities to all participants. All funds held under the plan are available to provide benefits to any participant. Accordingly, it is not possible in such a case to allocate actual contributions to specific participants.

Section 1.403(b)-1(d)(4) of the Income Tax Regulations, relating to certain tax sheltered annuities, provides that if, for any employee, the actual amounts of employer contributions to a defined benefit plan are not known, such amounts are to be determined under the formula set forth in the regulations or under any other method utilizing recognized actuarial principles that are consistent with the provisions of the plan under which the contributions are made and the method adopted by the employer for funding the benefits under the plan.

The formula set forth in section 1.403(b)-1(d)(4) of the Regulations provides that the contributions made by the employer for the benefit of the employee as of the end of any taxable year, if not known, shall be deemed to be the product of the following four amounts:

(i) The projected annual amount of the employee's pension as of the end of the taxable year to be provided at normal retirement age from employer contributions, based upon

the plan provisions and assuming the employee's continued employment with his current employer at the current salary.

(ii) The value, from Table I at “normal retirement age” as defined in the plan, of an annuity of $1.00 per annum payable in equal monthly installments during the life of the employee.

(iii) The amount from Table II (representing the level annual contribution that will accumulate to $1.00 at normal retirement age) for the sum of (a) the number of years remaining from the end of the taxable year to normal retirement age, and (b) the lesser of the number of years of service credited through the end of the taxable year or the number of years that the plan has been in existence at such time.

(iv) The lesser of the number of years of service credited through the end of the taxable year or the number of years that the plan has been in existence at such time.

The source of the pension payments that A receives from the Plan can be determined by starting with the formula set forth in section 1.403(b)-1(d)(4) of the Regulations. First, determine the total amount of Employer’s deemed contributions to the Plan for A (“Total Contributions”) by calculating the product of: (i) A’s annual pension benefit from the Plan; (ii) the value from Table I that corresponds to the “normal retirement age” as defined by the Plan; (iii) the value from Table II that corresponds to the sum of (a) the number of years remaining from the end of the taxable year to normal retirement age, and (b) the lesser of the number of years of service credited through the end of the taxable year or the number of years that the Plan has been in existence at such time; and (iv) A’s total years of service.

Next, allocate Total Contributions between A’s Y months of service within the United States and Z months of service outside the United States. Multiply Total Contributions by Y/(Y+Z) to determine Employer’s deemed contributions with respect to A’s services within the United States (“US Contributions”) and by Z/(Y+Z) to determine Employer’s deemed contributions with respect to A’s services outside the United States (“Foreign Contributions”).

Finally, allocate each pension payment as follows:

1) The portion that is attributable to Employer’s deemed contributions with respect to A’s services within the United States equals US Contributions divided by the product of the quantities described in subdivisions (i) and (ii) of section 1.403(b)-1(d)(4) of the Regulations.

2) The portion that is attributable to Employer's deemed contributions with respect to A's services outside the United States equals Foreign Contributions divided by the product of the quantities described in subdivisions (i) and (ii) of section 1.403(b)-1(d)(4) of the Regulations.

3) The portion that is attributable to earnings of the Plan with respect to A equals the remainder of the payment.

CONCLUSION

Based solely on the information submitted and on the representations made by A, we conclude that the portion of A's pension that is treated as income from sources within the United States should be determined under the principles of Revenue Ruling 79-388. An amount that is attributable to deemed employer contributions should be determined using the formula set forth in section 1.403(b)-1(d)(4) of the Income Tax Regulations. Such amount should be allocated between U.S. source and foreign source on the basis of where A performed the relevant services. The remainder should be treated as earnings and accretions that represent income from U.S. sources.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter. No opinion is expressed concerning the tax treatment of the pension payments under other provisions of the Code and regulations, or the tax treatment of any condition existing at the time of, or effects resulting from, the pension payments that are not specifically addressed above.

Pursuant to Section 11.04 of Rev. Proc. 2004-1, 2004-1 I.R.B. 1, a letter ruling found to be not in accord with the current views of the Service may be revoked or modified. A letter ruling may be revoked or modified due to, among other things, the issuance of regulations or a revenue ruling, revenue procedure, notice or other statement published in the Internal Revenue Bulletin. If a letter ruling is revoked or modified, the revocation or modification applies to all years open under the period of limitations unless the Service uses its discretionary authority under section 7805(b) of the Code to limit the retroactive effect of the revocation or modification.

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

A copy of this letter must be attached to any income tax return to which it is relevant.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to the taxpayer.

Sincerely,

M. Grace Fleeman
Senior Counsel, Branch 1
Office of Associate Chief Counsel
(International)