Internal Revenue Service

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Department of the Treasury
Washington, DC 20224

Third Party Communication: None
Date of Communication: Not Applicable
Person To Contact:

Telephone Number:

Refer Reply To:
CC:TEGE:EB:EC
PLR-124215-08
Date:
October 21, 2008

In Re:

LEGEND:

Taxpayer =

Employee =

Organization =

Dear :

This letter is in response to a letter dated May 9, 2008, submitted by your authorized representative, requesting a ruling under section 404(a) of the Internal Revenue Code (Code). Specifically, you requested a ruling that naming a section 501(c)(3) organization as a beneficiary of your employee's deferred compensation will not preclude the deduction of the compensation pursuant to section 404(a)(5). The facts, as represented, are as follows.

Taxpayer is a corporation that adopted a nonqualified deferred compensation plan (Plan) for a group of highly compensated employees. The Plan allows employees to defer a specified percentage or dollar amount of their salary and incentive compensation. The deferred compensation in the Plan becomes payable upon the employee's death, separation from service, or upon termination of the Plan. Each employee may designate in writing one or more beneficiaries to receive all or part of the employee's deferred compensation in the event of the employee's death.

Employee is employed by Taxpayer and participates in the Plan. Spouse (Employee's spouse) was designated by Employee as the beneficiary of the deferred compensation if Spouse survives Employee by 45 days and does not disclaim the compensation. If Spouse does not survive Employee by 45 days or disclaims the deferred compensation, Employee designated Organization, a section 501(c)(3) organization, as the beneficiary.

Section 404(a) of the Code provides that if compensation is paid or accrued on account of any employee under a plan deferring the receipt of such compensation, the compensation is not deductible under Chapter 1 of Subtitle A of the Code when accrued. However, if the compensation would otherwise be deductible under Chapter 1 of Subtitle A of the Code, it is deductible under section 404 of the Code, subject to the limitations imposed by section 404.

Section 404(a)(5) generally provides that compensation paid under a nonqualified plan of deferred compensation (i.e., a plan for which contributions are not deductible under section 404(a)(1), (2), or (3) of the Code) is deductible in the taxable year in which an amount attributable to the contribution is includible in the gross income of employees participating in the plan. Section 1.404(a)-(12)(b) of the Income Tax Regulations provides that a contribution is includible “where the employee or his beneficiary excludes it from his gross income under section 101(b) or subchapter N.” Thus, this section illustrates that a contribution is considered includible in the gross income of an employee when it is includible in the gross income of the employee or his beneficiary, and a contribution is considered to be so includible even if it is excluded from the gross income of the beneficiary.

Section 691(a)(1) provides that the amount of all items of gross income in respect of a decedent which are not properly includible in respect of the taxable period in which falls the date of his death or a prior period (including the amount of all items of gross income in respect of a prior decedent, if the right to receive such amount was acquired by reason of the death of the prior decedent or by bequest, devise, or inheritance from the prior decedent) shall be included in the gross income, for the taxable year when received, of: (A) the estate of the decedent, if the right to receive the amount is acquired by the decedent's estate from the decedent; (B) the person who, by reason of the death of the decedent, acquires the right to receive the amount, if the right to receive the amount is not acquired by the decedent's estate from the decedent; or (C) the person who acquires from the decedent the right to receive the amount by bequest, devise, or inheritance, if the amount is received after a distribution by the decedent's estate of such right.

Section 691(a)(2) provides that if a right, described in section 691(a)(1), to receive an amount is transferred by the estate of the decedent or a person who received such right by reason of the death of the decedent or by bequest, devise, or inheritance from the decedent, there shall be included in the gross income of the estate or such person, as the case may be, for the taxable period in which the transfer occurs, the fair market value of such right at the time of such transfer plus the amount by which any consideration for the transfer exceeds such fair market value. For purposes of section 691(a)(2), the term “transfer” includes sale, exchange, or other disposition, or the satisfaction of an installment obligation at other than face value, but does not include transmission at death to the estate of the decedent or a transfer to a person pursuant to the right of such person to receive such amount by reason of the death of the decedent or by bequest, devise, or inheritance from the decedent.

Section 691(a)(3) provides that the right, described in section 691(a)(1), to receive an amount shall be treated, in the hands of the estate of the decedent or any person who acquired such right by reason of the death of the decedent, or by bequest, devise, or inheritance from the decedent, as if it had been acquired by the estate or such person in the transaction in which the right to receive the income was originally derived and the amount includible in gross income under section 691(a)(1) or (2) shall be considered in the hands of the estate or such person to have the character which it would have had in the hands of the decedent if the decedent had lived and received such amount.

Section 1.691(a)-1(b) of the regulations provides that, in general, the term “income in respect of a decedent” refers to those amounts to which a decedent was entitled as gross income but which were not properly includible in computing his taxable income for the taxable year ending with the date of his death or for a previous taxable year under the method of accounting employed by the decedent. See the regulations under section 451.

Section 1.691(a)-4(a) provides the rules governing the treatment of income in respect of a decedent (or a prior decedent) in the event a right to receive such income is transferred by the estate or person entitled thereto by bequest, devise, or inheritance, or by reason of the death of the decedent. In general, the transferor must include in his gross income for the taxable period in which the transfer occurs the amount of the consideration, if any, received for the right or the fair market value of the right at the time of the transfer, whichever is greater. Thus, upon a sale of such right by the estate or person entitled to receive it, the fair market value of the right or the amount received upon the sale, whichever is greater, is included in the gross income of the vendor. Similarly, if such right is disposed of by gift, the fair market value of the right at the time of the gift must be included in the gross income of the donor. In the case of a satisfaction of an installment obligation at other than face value, which is likewise considered a transfer under section 691(a)(2), see section 1.691(a)-5.

Section 1.691(a)-4(b) provides that if the estate of a decedent or any person transmits the right to income in respect of a decedent to another who would be required by section 691(a)(1) to include such income when received in his gross income, only the transferee will include such income when received in his gross income. In this situation, a transfer within the meaning of section 691(a)(2) has not occurred.

Section 2518 provides, in general, that if a person makes a qualified disclaimer with respect to any interest in property, Subtitle B shall apply with respect to such interest as if the interest had never been transferred to such person.

Section 2518(b) provides that the term “qualified disclaimer” means an irrevocable and unqualified refusal by a person to accept an interest in property but only if, (1) such refusal is in writing, (2) such writing is received by the transferor of the interest, his legal representative, or the holder of the legal title of the property to which the interest relates, (3) such person has not accepted the interest or any of its benefits, and (4) as a result of such refusal, the interest passes without any direction on the part of the person making the disclaimer and passes either, (A) to the spouse of the decedent, or (B) to a person other than the person making the disclaimer.

Based solely on the facts presented, we rule as follows:

If Spouse makes a qualified disclaimer with respect to Employee's deferred compensation or predeceases the Employee, then naming Organization as the designated beneficiary of the deferred compensation will not preclude Taxpayer's deduction of the compensation pursuant to section 404(a)(5).

No opinion is expressed concerning when the Employee's deferred compensation will be deductible or includible in gross income. Except as specifically ruled above, no opinion is expressed as to the federal tax consequences of the transaction described above under any other IRC provision. The ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) provides that it may not be used or cited as precedent. A copy of this letter should be attached to any of your income tax returns to which it is relevant.

The rulings contained in this letter are 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 rulings, it is subject to verification on examination.

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

Sincerely,

John B. Richards
Acting Senior Technician Reviewer
Executive Compensation Branch
Office of Division Counsel /
Associate Chief Counsel /
Tax Exempt & Government Entities

Enclosures:
Copy of letter
Copy for section 6110 purposes